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Export Financing Options for NAFTA Country Businesses

*Roland P. Wiederaenders, III**

I. Introduction.

Governmental export financing agencies and the programs they offer are oft-times essential to businesses engaging in exporting activities, as financing for exporting transactions is frequently not available from commercial banks due to the risk inherent in exporting activities. A great deal of competition exists among the developed nations for foreign export markets, and while seventy-three countries offer export credit agencies, the Group of Seven (G7) industrial nations extend about half of all export financing credits worldwide.¹ The world economy is becoming increasingly integrated, and the competition for export markets will most likely expand in the coming years. As this integration continues, businesses will demand more extensive governmental assistance in financing export-related business activities.

Governmental agencies offer a variety of export financing options. The type of financing most commonly available is direct lending, where foreign buyers of exports can obtain financing for their purchases from a governmental agency in the exporter's home country.

Another means of financing export transactions is through letters of credit, which generally are divided into two categories—commercial letters of credit and stand-by letters of credit. Letters of credit are useful in international transactions because they reduce both the risk created by the exporter's inability to properly evaluate his foreign buyer's credit-

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1. *Hearings on Export-Import Bank Reauthorization Before Subcomm. on Int'l Fin., Senate Comm. on Banking, Housing and Urban Affairs*, 105th Cong. (1997) (statement of Ms. JayEtta Hecker, Assoc. Dir., Int'l Relations and Trade Issues, Natl. Security and Int'l Affairs Div.), available in 1997 WL 11235073 [hereinafter "Hecker"].

worthiness, and also the risks associated with foreign exchange.² A commercial letter of credit is the kind typically used in international sale of goods transactions and the type generally referred to in this paper.

Project financing is another means by which an export transaction might be financed. Project financing refers to the financing of projects that are dependent upon project cash flows for repayment. Project financing has been used in the past for oil and gas mining and the construction of power projects. Developing countries are privatizing industries that were previously held by their governments; for this reason, new opportunities for project financing should arise in areas such as telecommunications and transportation. The availability of project financing should facilitate an exporter's ability to take advantage of these opportunities.

Apart from direct lending activities and project financing, another financing option offered by these governmental agencies is the provision of working capital loans to exporters for the financing of their export transactions.

In addition to providing credit for exporting activities, many agencies offer guarantee programs for loans underwritten by private lending institutions. These guarantees give private lending institutions additional security in their underwriting of loans for the financing of export transactions; loans that are generally too risky for banks to make without such guarantees. In addition to such guarantees, many agencies offer insurance policies that allow exporters and investors to guard against the risk of loss due to political violence occurring in the countries to which they are exporting.

In addition to these services, this paper discusses several governmental agencies that offer financing for market development activities undertaken by firms that are considering entering the exporting business.

2. ROGER D. WIEGLEY, *EXPORT & TRADE FINANCE* 1-1 (1996). Regarding the exchange risk:

The credit of the issuing bank, as well as the credit of any confirming bank, stands behind the letter of credit. On the question of foreign exchange, many developing countries allow local banks to use hard currency to cover trade obligations even when foreign exchange is otherwise restricted. Trade transactions usually have a high priority in the economic planning of developing countries. Moreover, a bank opening a letter of credit in the importer's country will first assure itself to the extent possible that the required foreign exchange will be made available by the central bank or other monetary authority when payment is due. Failure to make such payment would severely damage the bank's international credit standing.

Id. at 1-2. Regarding the risk associated with the exporter's inability to evaluate his importer's creditworthiness:

The letter of credit is issued by the bank on behalf of the buyer, and the bank makes a separate contractual arrangement with the buyer to obtain reimbursement from the buyer after payment is made to the seller under the letter of credit. The letter of credit is a promise by the issuing bank to make payment if the seller conforms exactly to the conditions set forth in the letter of credit. In most commercial transactions, these conditions require the seller to present certain documents such as a negotiable bill of lading, insurance documents and invoices. If the seller ships the exporter[s] goods in accordance with its agreement with the customer, it will have the required documentation to obtain payment under the letter of credit. Thus the letter of credit substitutes the credit of the issuing bank for that of the buyer.

Id. at 1-2.

Integration of markets in the Western Hemisphere is only facilitated by the presence of bilateral and multilateral trade agreements, in particular, the NAFTA. As the NAFTA provisions continue to take effect, businesses in the Western Hemisphere will see exporting as an attractive way to expand their operations and will increasingly look to export financing to fund their exporting activities. The focus of this paper is to examine export financing facilities provided by the governments of the three NAFTA countries: the United States, Mexico, and Canada, along with some of the private export financing options available in these countries.

II. International Agreement Affecting Export Financing Options: Organization for Economic Cooperation and Development's Arrangement on Guidelines for Officially Supported Credits.

Before specifically discussing the NAFTA countries' export financing agencies and the programs they offer, a discussion of the Organization for Economic Cooperation and Development (OECD) and its influence on export financing is in order. Created in 1960, the OECD is a twenty-nine country international organization created for the purpose of facilitating a coordination of economic policy among its member states.³ With respect to export financing, the OECD serves as a forum for "negotiating limitations on government export credit subsidies and developing guidelines for export-financing assistance programs."⁴

Since the late 1970s, the OECD has attempted to reduce government involvement in these programs.⁵ In 1978, the OECD formalized a document called the "Arrangement on Guidelines for Officially Supported Export Credits."⁶ The Arrangement originally prescribed the following requirements for export credit agencies: minimum interest rates of seven to eight percent, required minimum down payments of fifteen percent, and "standardized repayment schedules, common reporting procedures, prior notification for derogation [from OECD standards], and maximum terms of repayment of 8.5 years for OECD nations and ten years for [less developed countries], LDCs."⁷

Subsequent changes to the Arrangement occurred, and in 1983, a new agreement changed many of the 1978 Arrangement's provisions. The new agreement, raising minimum interest rates to a level of ten to twelve percent, mandated an automatic semiannual adjustment of minimum rates for low-interest-rate countries, provided for the negotiated adjustment of rates for high-interest-rate countries, increased minimum rates, and reclassified a number of countries into more restrictive categories.

3. Hecker, *supra* note 1.

4. *Id.* "The OECD's 'Arrangement on Guidelines for Officially Supported Export Credits,' which was established in 1978, sets the terms and conditions for official export credits." *Id.* See also WIEGLEY, *supra* note 2, at VI-1. "OECD was formed to create uniform guidelines for governmental assistance for exports, thereby preventing 'auctions' in which ECA's [official credit support agencies] would be forced to bid against each other by offering evermore favorable terms to enable exporters in their respective countries to win sales in competitive situations." *Id.*

5. Hecker, *supra* note 1.

6. See generally Andrew M. Moravcsik, *Disciplining Trade Finance: the OECD Export Credit Arrangement*, 43 INT'L ORG. 173, 181 (1989).

7. *Id.*

The OECD has continued to make attempts toward a reduction and eventual elimination of subsidized export finance programs available to OECD member states' firms.⁸ One of the United States' main achievements in ongoing OECD negotiations has been an agreement to ensure that interest rates offered by all nations' export credit agencies are market-based and above the cost of funds to governments.⁹ These base interest rates are adjusted monthly to keep up with market interest rate developments.¹⁰ Presently, OECD member states have entered into an agreement that has further standardized and set more stringent minimum fees (beginning in 1999) for all member country export credit agencies.¹¹ While the agreement has potential for reducing the permissible level of government subsidies available for these programs, any reduction may contravene the facilitation of export driven economic development of OECD member states that export finance programs facilitate.¹²

III. Export Financing Options for United States Firms.

A. UNITED STATES FEDERAL AGENCIES.

1. *Ex-Im Bank*.

a. *Ex-Im Bank History and General Overview of Programs*.

Created in 1934, the Ex-Im Bank is an independent U.S. Government agency created with facilitation of export financing as its primary objective.¹³ It operates under a renewable congressional charter that expires annually on September thirtieth.¹⁴ In its operations, Ex-Im Bank must abide by certain statutory requirements.¹⁵ Primary among these requirements, Ex-Im Bank is directed to provide financing programs at:

rates and on terms and other conditions which are fully competitive with the Government-supported rates and terms and other conditions available for the financing of exports of goods and services from the principal countries whose exporters compete with United States exporters.¹⁶

8. Hecker, *supra* note 1.

9. *Hearings on Export-Import Bank Reauthorization, Before Comm. on Banking and Fin. Services, Subcomm. on Domestic and Int'l Monetary Pol'y*, 105th Cong. (1997) (statement of Ms. Meg Lundsager, Treas. Dep. Asst. Secretary for Trade and Investment Pol'y), available in 1997 WL 10570572 [hereinafter "Lundsager"].

10. *Id.*

11. Hecker, *supra* note 1. The minimum fees are established according to country risk ratings established by the OECD. *Id.*

12. *Id.*

13. *Id.* See also *Hearings on Export-Import Bank Reauthorization, Before House Comm. on Banking and Fin. Services, Subcomm. on Domestic and Int'l Monetary Pol'y*, 105th Cong. (1997) (statements of Mr. Benjamin F. Nelson, Security and Int'l Affairs Dev., U.S. GAO), available in 1997 WL 10570571 [hereinafter "Nelson"].

14. Nelson, *supra* note 13.

15. *Id.*

16. 12 U.S.C.A. § 635(b)(1)(A) (1997).

In addition to this requirement, the Ex-Im Bank is to "seek to minimize competition in government-supported export financing and shall in cooperation with other . . . [U.S.] Government agencies, seek to reach international agreements to reduce government subsidized export financing."¹⁷ Ex-Im Bank is also directed to "supplement and encourage, [but] not compete with, private capital" in the financing of businesses' exporting activities.¹⁸

According to Ex-Im Bank, the exports that it financed in 1996 "supported or maintained" nearly 300,000 jobs in the United States.¹⁹ During the fiscal years of 1994 to 1996, the Ex-Im Bank provided on average per year \$12.8 billion in export financing commitments, which included loans, guarantees, and insurance; annual average program cost was \$877 million.²⁰ For fiscal year 1997, Ex-Im estimates that it will provide an all-time high of \$16.5 billion in export financing through its various programs. Program costs are projected to fall from \$934 million in fiscal year 1996 to \$773 million in fiscal year 1997 and to \$681 million in fiscal year 1998. This decrease is due to a projected increase in lower-risk financing, such as project finance and aircraft transactions.²¹

b. Justifications for Ex-Im Bank.

Supporters of Ex-Im Bank offer several arguments in favor of Ex-Im Bank's continued existence. One justification for Ex-Im Bank is the competition U.S. exporters face from foreign exporters who have similar programs made available to them by the governments of their respective countries.²² The standard argument is that U.S. exporters will not be able to compete unless they have similar resources as their foreign competitors.

Related to this justification, Ex-Im Bank itself claims that the market does not always efficiently allocate resources and that these "market failures" justify the programs Ex-Im Bank provides. Among these market failures, Ex-Im Bank cites the following:

- Private financial institutions may be unwilling to support exports to emerging markets even when the risk is correctly priced.
- Foreign buyers in certain markets may be unable to secure long-term financing for capital equipment.
- Finally, and probably the most often-cited example, is that small business exporters may have difficulty in obtaining export financing.²³

Opponents of Ex-Im Bank, however, claim that Ex-Im Bank is mere "corporate welfare," and does not enable substantive economic growth.²⁴

17. *Id.*

18. 12 U.S.C.A. § 635(b)(1)(B) (1997).

19. Nelson, *supra* note 13 (citing KEEPING AMERICA COMPETITIVE: 1996 EX-IM BANK ANNUAL REPORT 5 (1996)).

20. *Id.*

21. *Id.*

22. Hecker, *supra* note 1.

23. *Id.*; see also Nelson, *supra* note 13.

24. Hecker, *supra* note 1.

c. Ex-Im Bank's Programs.

(i) *Domestic Content Requirement and Eligibility Criteria.*

All Ex-Im Bank programs have minimum acceptance levels and varying coverage for foreign content included in U.S. manufactured and produced items.²⁵ Specific programs provide eligibility requirements for foreign content included in the manufactured items. Regarding eligible foreign content requirements, when ten to fifteen percent of the manufactured item contains eligible foreign content, financing is available for the total contract price less a fifteen percent cash down-payment. When fifteen to fifty percent of the manufactured item consists of eligible content, the exporter can obtain financing for only the U.S. content. Ex-Im Bank is statutorily required to "set aside" up to ten percent of its business for small businesses. Almost all programs are subject to an evaluation assessing the environmental impact of the financed project. Ex-Im Bank is required to provide financing only for U.S. goods and services shipped on U.S. vessels.²⁶

For all direct loans and long-term guarantees, items must be shipped on U.S. bottoms. If the goods are shipped on non-U.S. bottoms, the goods are ineligible for Ex-Im Bank support unless the U.S. Maritime Administration provides a waiver of these requirements. There are three waiver types: the General Waiver, where up to fifty percent of the goods may be shipped on non-U.S. vessels; the Hardship Waiver, available if no U.S. vessels are scheduled for the destination; and the Country Waiver, where Brazil applies to eligibility of shipping costs not counting towards the General Waiver provision.²⁷

The primary programs through which Ex-Im Bank provides support include: Medium and Long Term Direct Loans and Guarantees; Project Finance; Credit Guarantee or Financial Institution (Bank) Facilities; Aircraft Finance Program; Insurance Program; and Working Capital Guarantee Program.

(ii) *Medium and Long Term Direct Loan Programs.*

(A) *General Requirements.*

Through its Medium and Long Term Loans and Guarantee programs, Ex-Im Bank offers fixed-rate loans directly to foreign buyers of U.S. goods and services.²⁸ Through these loans, Ex-Im Bank seeks to fill in gaps in the availability of private export financing.

25. See Ex-Im Bank's web-page (visited Feb. 17, 1998) <<http://www.exim.gov/mover.html>>. Much of the discussion regarding Ex-Im Bank also comes from materials provided to the author by Ex-Im Bank. For a good detailed overview of Ex-Im Bank programs, apart from Ex-Im Bank's web-page itself, see WIEGLEY, *supra* note 2, at V-1 through V-97 and WILLIAM P. STRENG & JESWALD W. SALACUSE, *INTERNATIONAL BUSINESS PLANNING: LAW AND TAXATION (UNITED STATES)* § 10.01[A] (1997).

26. For this discussion of domestic content requirement, see Ex-Im Bank's web-page (visited Feb. 17, 1998) <<http://www.exim.gov/mover.html>>.

27. Borrowers are to address waiver requests to the Director, Office of Market Development, Maritime Administration, U.S. Department of Transportation, 400 7th Street S.W., Washington, D.C. 20590. *Id.*

28. This discussion of Ex-Im Bank's Medium & Long Term Programs comes verbatim from Ex-Im Bank's web-cite (visited Feb. 17, 1998) <<http://www.exim.gov/mltprog.html>>.

Ex-Im Bank will loan to a U.S. exporter's foreign customer up to eighty-five percent of the U.S. export value, and the buyer must make a cash down payment to the U.S. exporter of at least fifteen percent of the U.S. export value. At the preliminary stage, Ex-Im Bank frequently offers the option of guarantee support or a direct loan.

Among the exports eligible to receive this financing are capital equipment, large-scale projects, and related services. Ex-Im Bank requires a certification from the exporter both stating that the goods and services being financed are of U.S. origin or manufacture, and also disclosing any commissions or fees other than those paid in the ordinary course of business. The goods must be transported by an ocean vessel of U.S. registry, unless the foreign buyer obtains a waiver of this requirement from the U.S. Maritime Administration.²⁹ Transportation costs for goods shipped on non-U.S. registered vessels or aircraft are considered foreign costs, even if the borrower has obtained the waiver. The borrower is required to obtain insurance against marine and transit hazards on all shipments of exports financed by an Ex-Im Bank loan. Borrowers should give U.S. insurers nondiscriminatory opportunity to bid for such insurance business. Premiums paid to U.S. insurers are eligible for Ex-Im Bank financing.

The borrower must be a creditworthy entity in a country eligible for Ex-Im Bank assistance and the borrower may be an entity other than the buyer. Generally, on government or government-sponsored projects, Ex-Im Bank will look for a host-government guarantee. Private sector borrowers may be considered on their own merits or may offer a creditworthy bank as a guarantor.

(B) *Characteristics and Repayment Terms.*

The fifteen percent cash down payment required may be paid in a lump sum before disbursement of the financing, or may be paid in installments equal to at least fifteen percent of the value of each completed shipment and related disbursement under the contract. The buyer and the seller negotiate this aspect of the agreement. To be eligible for Ex-Im Bank financing, the buyer must pay progress payments over the product manufacturing period or the project construction period, according to a purchase contract approved by Ex-Im Bank. The progress payments must bear a reasonable relationship to the amounts expended by the U.S. supplier.

The repayment terms on transactions supported by direct loans normally range from five to ten years, depending on the export value, the product or project being financed, the importing country, and the terms offered by officially supported competitors. Ex-Im Bank direct loans generally involve amounts over US\$10 million or have a repayment terms of five or more years. Transactions involving loan amounts of less than US\$10 million are normally financed by domestic financing institutions or third-party lenders, with Ex-Im Bank providing guarantees for this credit. The maximum repayment term is five years for relatively rich countries and ten years for relatively poor countries. Exceptions to these general guidelines exist by agreement among OECD countries. Payments are usually made in semi-annual installments and begin six months after final delivery, at the mid-point of deliveries, or at completion of the project, whichever is appropriate.

29. See *supra* note 27 for information regarding MARAD waiver.

(C) *Interest Rates and Finance Charges.*

Interest rates on direct loans are fixed for the life of the loan at the time of Ex-Im Bank's Final Commitment. Interest is payable on the installment dates on outstanding balances. Ex-Im Bank charges the minimum OECD rate applicable to the category of the importing country and the repayment period. There is a \$100 processing fee for each new application and for each application for a Final Commitment that is not a conversion. After Ex-Im Bank issues a Final Commitment, Ex-Im Bank charges a commitment and exposure fee. The amount of the commitment fee is equal to one-half of one percent per annum on the undisbursed balance of a direct loan. This fee begins to accrue sixty days after the date of the Final Commitment. The exposure fee is assessed on each disbursement of the direct loan and may be financed by Ex-Im Bank. The parties to the underlying transaction decide who will pay this fee and notify Ex-Im Bank of their determination at the time of application for final commitment. There are no charges imposed for legal services provided that Ex-Im Bank staff prepares the loan documents; however, in complex cases, Ex-Im Bank may hire outside counsel for the drafting. In such an instance, the borrower will pay all such legal fees.

(D) *Conditions Precedent to the Availability and Drawdown of the Loan.*

Before drawing down the loan, the borrower must satisfy the conditions precedent to the availability of the loan specified in the loan agreement. The buyer is usually required to provide Ex-Im Bank with such documents as promissory notes, evidence of the borrower's authority to enter into the loan agreement, a legal opinion, an acquisition list of the items to be financed, and a copy of any necessary authorizations from the authorities in the borrower's country. Once the borrower has complied with all of these conditions, Ex-Im Bank will make the loan available to the borrower.

Once these conditions have been satisfied, the borrower may request a drawdown. The drawdown request is made on a Request for Disbursement form (attached to the loan agreement), which must be accompanied by copies of the paid invoices, a Supplier's Certificate (also attached to the loan agreement), and copies of the bills of lading. In addition, it is a requirement of each drawdown that all exposure and commitment fees and other applicable costs and expenses required to be paid have been paid. The borrower also must not be in default under the loan agreement. Two procedures for the drawdown are available to the borrower.

The first of these two is in the form of a request for Ex-Im Bank to make disbursements to the borrowers account in a commercial bank in the United States as reimbursement for the financed portion of payments the borrower has made to the exporter.

The second of the two available procedures is a letter of credit. The borrower requests that a commercial bank (acceptable to Ex-Im Bank) in the United States issue, confirm, or advise letters of credit (L/C) in favor of the exporter. The L/C bank pays the exporter when presented with the documents specified in the letter of credit. Ex-Im Bank reimburses the L/C bank for Ex-Im Bank's share of such payments.

Aggregate drawdowns under the agreement cannot exceed the percentage of the eligible U.S. costs specified in the loan agreement and financed under the loan.

(iii) *Project Finance.*

Ex-Im Bank also makes a limited recourse project finance program available.³⁰ Financed projects do not rely on the typical export credit agency security package that has recourse to a foreign government, a financial institution, or an established corporation to

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30. The discussion of Ex-Im Bank's Project Finance program comes verbatim from Ex-Im Bank's web-site (visited Feb. 17, 1998) <<http://www.exim.gov/mpfprogs.html>>. Ex-Im Bank's web-site provides specific Project Criteria Requirements:

I. General Project

The project should have long-term contracts from credit worthy entities for the purchase of the project's output and the purchase of the project's major inputs such as fuel, raw materials, and operations and maintenance. Such contracts should extend beyond the term of the requested Ex-Im Bank financing. In sectors such as telecommunications and petrochemicals if longer term contracts are not available, Ex-Im Bank will evaluate the transactions on a case-by-case basis, looking for economically compelling business rationale.

The project should contain an appropriate allocation of risk to the parties best suited to manage those risks. Sensitivity analysis should result in a sufficient debt service coverage ratio to ensure uninterrupted debt servicing for the term of the debt.

Total project cost should be comparable to projects of similar type and size for a particular market.

Product unit pricing and costs should reflect market based pricing.

Devaluation risk needs to be substantially mitigated through revenues denominated in hard currencies, revenue adjustment formulas based on changing currency relationships, or other structural mechanisms.

...

II. Participants

Project sponsors, offtake purchasers, contractors, operators, and suppliers must be able to demonstrate the technical, managerial and financial capabilities to perform their respective obligations within the project.

...

III. Technical

Project technology must be proven and reliable, and licensing arrangements must be contractually secured for a period extending beyond the term of the Ex-Im Bank financing.

A technical feasibility study or sufficient[ly] detailed engineering information needs to be provided to demonstrate technical feasibility of the project.

...

IV. Host Country Legal/Regulatory Framework & Government Role

Host government commitment to proceeding with the project needs to be demonstrated.

Legal and regulatory analysis needs to demonstrate that the country conditions and the project structure are sufficient to support long-term debt exposure for the project through enforceable contractual relationships.

Ex-Im Bank's relationships with the host government will be addressed on a case-by-case basis. An Ex-Im Bank Project Incentive Agreement (PIA) with the host government may be required. The PIA addresses certain political risks and Ex-Im Bank's method of resolution of conflict with the host government pertaining to these issues. Only certain markets will require a PIA.

Id.

meet a reasonable assurance of repayment criterion. To be successful, these projects rely on a large number of integrated contractual arrangements, as well as the country's legal framework and investment environment. Ex-Im Bank estimated that project-financing deals will account for about thirty percent of its total financing in fiscal year 1997, whereas this financing only accounted for fourteen percent of its total assistance in 1996.³¹

In appropriate circumstances, Ex-Im Bank will offer the maximum support allowed within the rules of the OECD Arrangement.³² This support includes the following: financing of interest on the Ex-Im Bank financing during the construction period of the project; allowance of up to fifteen percent foreign content in the U.S. package; financing of host-country local costs of up to fifteen percent of the U.S. contract subject to Ex-Im Bank local cost support criteria; and the maximum repayment term allowed under OECD guidelines.

There are no minimum or maximum size limitations to the projects being financed. There are also no predetermined equity requirements, however equity must be in cash-equivalent form. Ex-Im Bank will review and determine appropriate equity structures on a case-by-case basis. The equity sponsor's ownership position cannot be transferred without Ex-Im Bank's consent. Ex-Im Bank will not consider the contribution of development fees and similar contributions as "equity at risk." Also, Ex-Im Bank will carefully review development costs when determining "equity at risk." If Ex-Im Bank cannot definitively determine the sponsor's creditworthiness, Ex-Im Bank may require a letter of credit from a prime bank.

Any combination of either direct loans or guarantees for commercial bank loans with political risk only or comprehensive coverage are available for a given project. During the construction period, Ex-Im Bank provides guarantees to cover only risk of loss due to political violence, expropriation, and transfer risk related to the project.

Exposure Fees vary depending on the risk assessment of the project. The Exposure Fee is payable in two phases: first, on a disbursement-by-disbursement basis during pre-completion, and then, at the disbursement of permanent financing at project completion. Should Ex-Im Bank support become unnecessary, the second phase of the Exposure Fee will not be payable.

Ex-Im Bank's environmental procedures and guidelines will apply to the Project Financing. All applicants must submit a Preliminary Environmental Assessment report, conducted by an independent third party expert prior to an application for a final commitment.³³

31. See Nelson, *supra* note 13.

32. For a good discussion of the OECD Arrangement on Guidelines for Officially Supported Export Credits, see generally Moravcsik, *supra* note 6.

33. "Unlike the U.S. Ex[-Im B]ank, EDC [Canada's governmental export development bank, see *infra*] does not have to do an environmental impact assessment of projects. Thus, while the U.S. agency has made a 'preliminary decision' not to finance the controversial Three Gorges dam in China on environmental grounds," the EDC is providing close to US\$170 million for this project. Sheldon Gordon, *Worldly Ambition: As Export Development Corp.'s new CEO, Ian Gillespie is Expected to Turn a Profit While Supporting Canadian Sales Around the Globe. And Who Could Have a Problem with That?*, THE FIN. POST, Feb. 1, 1998, at 20, 1998 WL 7189948.

With the assistance of outside financial advisors,³⁴ Ex-Im Bank will provide preliminary indication of support, called a Preliminary Project Letter (PPL), within forty-five days from the date evaluation begins by the outside consultant. Should the project be sufficiently developed, the sponsor may proceed directly to a Final Commitment from the PPL, as determined by the Project Finance Division. Finance and security documents must be subject to New York law.

Ex-Im Bank will consider project finance transactions in countries closed to traditional support due to economic conditions. The applicant, however, must present risk mitigants in order for such projects to be considered. An example of such risk mitigants are offshore escrow accounts of hard currency revenues with host government approvals. The exposure fee charged by Ex-Im Bank will reflect the project and the inherent market risk. If a government-owned utility or parastatal is the primary offtaker, Ex-Im Bank's Country Limitation Schedule will dictate if cover is available.

Ex-Im Bank is looking for shareholders with significant experience and real equity at risk throughout the amortization of Ex-Im Bank coverage. While Ex-Im Bank's statutory mandate is to provide export financing support when the private market is unwilling or unable to do so because of the risk, it nonetheless requires a significant commitment on the part of the applicant.

(iv) *Ex-Im Bank Export Credit Insurance Program.*

Ex-Im Bank's Export Credit Insurance Program assists U.S. exporters in developing and expanding their overseas sales by protecting them against loss due to default by their foreign buyer or loss due to political or other commercial reasons.³⁵ The Ex-Im Bank policy facilitates an exporter's ability to obtain export financing; with prior approval by Ex-Im Bank, the proceeds of the policy can be assigned to a financial institution as collateral. The policies Ex-Im Bank issues are flexible—they may insure shipments to one buyer or to many buyers; insure comprehensive (commercial and political) credit risks or only specific political risks; or cover short-term as well as medium-term sales. Three separate policies are geared specifically to a small business starting out in export sales; these are the Small Business Policy, the Small Business Environmental Policy, and the Umbrella Policy. Eligibility criteria differ for each type of policy.

34. Ex-Im Bank's "financial advisors are: PMD International, Inc., Schrodgers and Taylor-DeJongh, Inc. Ex-Im Bank selects one of these advisory firms as its financial advisor for each transaction. While it is not required that the applicant retain its own financial advisor, it is highly recommended that an advisor with limited-recourse project finance experience be retained." Ex-Im Bank's web-page *supra* note 30.

35. This discussion of Ex-Im Bank's Export Credit Insurance Program comes verbatim from Ex-Im Bank's website (visited Feb. 17, 1998) <<http://www.exim.gov/minsprog.html>>. Ex-Im Bank notes that, for these policies, "[c]overage against political risks only is limited and does not cover devaluation of a foreign currency as a risk of default. As the overwhelming majority of losses result from commercial default, the exporter should consider the appropriateness of obtaining a comprehensive (commercial and political risks coverage) policy. A political risks only policy is not subject to a first loss deductible." *Id.*

(v) *Working Capital Guarantee Program.*

(A) *General Description.*

Ex-Im Bank's Working Capital Guarantee Program is designed to encourage commercial lenders to make loans to U.S. businesses for various export-related activities.³⁶ The Program helps small and medium-sized businesses that have exporting potential, but need funds to buy or produce goods, and/or to provide services, for export. It may be used to cover working capital loans to a U.S. business made by a private lender provided that the lender shows that the loan would not have been made without Ex-Im Bank's guarantee, and Ex-Im Bank determines that the exporter is creditworthy.

The exporter may use the guaranteed financing to do the following: purchase raw materials and finished products for export; pay for materials, labor, and overhead to produce goods; provide services for export; and cover standby letters of credit serving as bid bonds, performance bonds, or payment guarantees. For companies in the service sector, costs such as engineering, design, and allocable overhead may be financed under this program. The loan can be structured to finance one or more specified transactions, or as a revolving line of credit.

Ex-Im Bank's working capital guarantee covers ninety percent of the loan's principal and accrued interest. Guaranteed loans must be fully collateralized at all times. Acceptable collateral may include export-related inventory, export-related accounts receivable or other assets. Inventory purchased with disbursements under the Ex-Im Bank guaranteed loan may be used as collateral, as may the accounts receivable generated from the transactions supported.

Exporters must demonstrate a successful history of past performance, including at least one full year of operations and a positive net worth. Financial statements must show sufficient strength to accommodate the requested debt.

(B) *Application Procedures.*

Exporters may apply directly to Ex-Im Bank for a preliminary commitment for a guarantee. If approved, the exporter then approaches various lenders to secure the most attractive loan package. A preliminary commitment is valid for six months and the lender applies for the final commitment.

Ex-Im Bank imposes no interest rate ceilings or maximum fee limitations; however, lenders should take into account that ninety percent of the risk is covered by an agency of the U.S. Government and price their loans accordingly.

Ex-Im Bank charges a processing fee of \$500 with each application for a preliminary commitment, \$400 of which will be applied toward the Facility Fee on the operative final commitment, if any, or a processing fee of \$100 with each application for a final commitment. No additional fee is charged for conversion of a preliminary commitment to a final commitment. An up-front Facility Fee of 1.5% of the total loan amount also is charged, and is based on a one-year loan. For loans of up to six months, the Facility Fee is 0.75% of the total loan amount.

36. This discussion of Ex-Im Bank's Working Capital Guarantee Program comes verbatim from Ex-Im Bank's web-page (visited Feb. 17, 1998) <<http://www.exim.gov/wcgp.html>>.

(C) *Accelerated Processing for Lenders.*

Ex-Im Bank offers lenders accelerated processing of requests through the Priority Lending Program (PLP) and Delegated Authority Program. Lenders must send two people to a one-week Ex-Im Bank seminar in order to qualify for either of these programs. Under the PLP, lenders who have made at least two transactions operative under the Working Capital Guarantee Program may submit a complete write-up of the exporter and transaction and be given a ten-day turnaround on their application. Since most of the work has already been done, Ex-Im Bank can make its decision sooner.

Since October 1994, Ex-Im Bank has given the Delegated Authority Program to qualified lenders, which allows them to commit to Ex-Im Bank's guarantee as soon as they have made their credit decision. No further analysis is done by Ex-Im Bank. As added incentives, Ex-Im Bank allows the lender to retain a portion of the Facility Fee and separately collateralize the unguaranteed portion.

(vi) *Aircraft Finance Program.*

Ex-Im Bank offers financial support for the export of new or used U.S. manufactured aircraft, including helicopters, under its loan, guarantee, and insurance programs. Direct sales and finance leases are the typical structures contemplated in Ex-Im Bank transactions. The terms and conditions of Ex-Im Bank's aircraft programs are generally governed by the OECD Sector Understanding on Export Credits for Civil Aircraft.³⁷

Large aircraft, which generally have over seventy seats in a passenger configuration, will be considered for financing on ten or twelve year repayment terms. Except for transactions that carry the repayment obligation of a sovereign government, Ex-Im Bank will require the financed aircraft as security for the transaction. As stipulated by the OECD, the maximum financed amount is eighty-five percent of the U.S. contract price; however, the financed amount may be reduced in cases where the risks are significant. Repayment may be structured according to a level principal or mortgage-style amortization. In all cases, Ex-Im Bank reserves the right to make the final determination on the profile of the debt repayment schedule.

An exposure fee of three percent for a guarantee or two percent for a direct loan, is assessed by Ex-Im Bank on its large aircraft transactions. The exposure fee may be included in the financed amount. The interest rate on Ex-Im Bank guaranteed loans is set by the commercial lender, and the interest rate on Ex-Im Bank direct loans is set according to the OECD. The commitment fee, which accrues on the unutilized loan availability, is one-half of one percent (0.005) for a direct loan and one-eighth of one percent (0.00125) for a loan guarantee.

Ex-Im Bank may allow the inclusion of spare parts in sovereign guaranteed large aircraft transactions. Generally, spare parts are not included in asset-based transactions; however, spare parts may be considered on a case-by-case basis when a substantial asset value to loan margin exists, and the airline is a suitable credit risk. Otherwise, spare parts can be considered in an application which is separate from the large aircraft financing.

The credit decision on small aircraft transactions rests solely upon the creditworthiness of the borrower or guarantor. Generally, asset-based financing structures for small air-

37. This discussion of Ex-Im Bank's Aircraft Finance Program comes verbatim from Ex-Im Bank's web-page (visited Feb. 17, 1998) <<http://www.exim.gov/afprogs.html>>.

craft are not eligible for Ex-Im Bank support. The exposure fee is determined by the term of the loan and the credit risk associated with the borrower or guarantor. The same commitment fees apply as for large aircraft.

Ex-Im Bank is prohibited, by law, from supporting the sale of military aircraft or civilian aircraft that will be used for military applications. All aircraft sales to military or quasi-military entities are considered to be for a military purpose. Exporters wishing to sell aircraft to military buyers must prove to Ex-Im Bank that such aircraft are intended to be used for a primarily civilian or humanitarian purpose. A limited waiver of the statutory prohibition from the State Department is available in cases where defense articles will be used for drug interdiction purposes.

Ex-Im Bank will consider financing the export from the United States of both large and small used aircraft on a case-by-case basis. The terms and conditions will differ from those cited above, and repayment terms will be shorter than the terms for comparable new aircraft.

2. *United States Trade and Development Agency.*

The U.S. Trade and Development Agency (TDA) is an independent agency of the U.S. Government whose stated goal is to assist in the creation of jobs for Americans by helping U.S. companies pursue overseas business opportunities.³⁸ The TDA primarily seeks to enable American businesses to compete for infrastructure and industrial projects in middle-income and developing countries. While not providing export financing *per se*, the TDA funds feasibility studies, orientation visits, specialized training grants, business workshops, and various forms of technical assistance.

Because of its objectives, the TDA only considers projects that have potential to mature into significant business opportunities for U.S. companies. There are several criteria a project must meet before it will be considered for TDA funding. First, the project must face strong competition from foreign companies that receive subsidies and other support from their governments. The project must also be a development priority of the country in which the project is located; regarding this requirement, the project must have the endorsement of the U.S. embassy in that nation. In addition to these requirements, the project must represent an opportunity for the sales of U.S. goods or services whose dollar amount is many times greater than the cost of TDA assistance. Finally, the project must be likely to receive implementation financing and must have a procurement process open to U.S. firms.

3. *Overseas Private Investment Corporation.*

The Overseas Private Investment Corporation (OPIC) plays an important role in helping U.S. firms reach expanding markets overseas.³⁹ Since beginning operation in 1971, OPIC has been the key U.S. Government agency encouraging American private business investment in developing countries, newly emerging democracies, and free market economies. Currently, OPIC programs are available for new and expanding business enterprises in some 140 countries and areas worldwide.

38. This discussion of the TDA comes verbatim from TDA's web-site (visited Jan. 3, 1998) <<http://www.tda.gov>>.

39. The discussion of programs offered by OPIC in large part comes verbatim from OPIC's web-site (visited Feb. 17, 1998) <<http://www.opic.gov>>.

OPIC assists American investors through four principal activities designed to promote overseas investment and reduce the associated risks of that investment: financing of businesses through loans and loan guaranties; supporting private investment funds which provide equity for U.S. companies investing in projects overseas; insuring investments against a broad range of political risks; and engaging in outreach activities designed to inform the American business community of investment opportunities overseas.

A self-sustaining agency, OPIC has recorded a positive net income for every year of operation, operates at no net cost to the U.S. taxpayer, and has accumulated reserves of more than \$2.6 billion. Since its inception, OPIC has supported investments worth nearly \$84 billion, generated \$43 billion in U.S. exports, and helped to create 200,000 American jobs. All of OPIC's guaranty and insurance obligations are backed by the full faith and credit of the United States of America.

OPIC supports, finances, and insures projects that have a positive effect on U.S. employment, are financially sound, and promise significant benefits to the social and economic development of the host country. OPIC will not support projects that could result in the loss of U.S. jobs, adversely affect the U.S. economy or the host country's development or environment, or contribute to violations of internationally recognized worker rights.

OPIC assistance is available for new investments, privatizations, and for expansions and modernizations of existing plants sponsored by U.S. investors. Acquisitions of existing operations are eligible if the investor contributes additional capital for modernization and/or expansion. There is no requirement that the foreign enterprise be wholly owned or controlled by U.S. investors. However, in the case of a project with foreign ownership, only the portion of the investment made by the U.S. investor is insurable by OPIC. Neither financing nor insurance will normally be available for investments in enterprises majority owned and controlled by a foreign government. Financing is not available for projects that can secure adequate financing from commercial sources.

Investments by OPIC clients may take many forms: conventional equity investments and loans; construction and service contracts; production sharing agreements; leases; various contractual arrangements such as consigned inventory, licensing, franchising, and technical assistance agreements; and other special agreements that investors may devise.

OPIC programs are generally available in the countries and areas currently appearing on the OPIC Country List. At times, statutory and policy constraints may limit the availability of OPIC programs in certain countries. Also, under agreements with certain countries, the host government may be required to approve OPIC assistance for a project. The approval procedures vary from country to country and are available from OPIC. Investors are urged to contact OPIC for up-to-date information regarding availability of OPIC services in specific countries, as well as information on program availability in countries not appearing on the OPIC Country List.

To receive OPIC support, projects must demonstrate a potential for positive effects on the U.S. economy. OPIC weighs the balance of payments and employment effects on the U.S. economy of every project it considers supporting. Such factors as the level of U.S. procurement, net financial flows, and net project exports to the United States are taken into consideration. Assistance is denied to projects that are likely to have a negative effect on U.S. employment or trade. OPIC will not support a "runaway plant," i.e., the substitution of existing U.S. facilities with a foreign plant to produce for the same U.S. or export markets. OPIC will decline to assist projects that are likely to have an adverse effect on the U.S.

balance of payments. OPIC assistance is not tied to the procurement of U.S. goods or services; however, OPIC encourages U.S. procurement, particularly from U.S. small businesses, wherever possible.

a. OPIC Project Finance.

One of the programs OPIC offers is project financing for ventures that involve significant equity and/or management participation by U.S. businesses. This project financing is accomplished through direct loans and loan guarantees. The OPIC carefully analyzes the economic, technical, marketing, and financial strength of each project, as OPIC expects repayment of the loans to occur from the cash flows generated by the projects, rather than by relying on sovereign or sponsor guaranties. There must be an adequate cash flow sufficient to pay overhead, to service all debt, and to provide the owners with an adequate return on their investments. Provided that these criteria are met, sponsors do not have to pledge their own general credit beyond the required completion undertakings. However, in ventures where project financing on these terms is impractical, OPIC will consider more conventional secured lending techniques.

Because OPIC's programs support private sector investments in financially viable projects, OPIC does not offer the same concessionary terms usually associated with government-to-government lending, nor does it typically offer financing of export sales unrelated to long-term investments in overseas business.

OPIC finances overseas ventures wholly owned by U.S. companies, as well as joint ventures in which the U.S. sponsor firm is a participant. The U.S. investor is expected to assume a meaningful share of the risk, generally through the purchase of at least twenty-five percent of the equity in the project. OPIC generally requires that at least fifty-one percent of the voting shares of the overseas venture be held by firms or persons from the private sector. However, financing may be offered to an entity in which government ownership of voting shares represents the majority, provided that contractually, management will remain in private hands and there is a strong showing of direct U.S. interest in other respects. Projects wholly owned by governments are not eligible.

Investors must be willing to establish sound debt-to-equity relationships that will not jeopardize the success of the project through insufficient equity or excessive leverage. The financial structure will vary with the nature of a specific business and will be affected by the variability of expected cash flows. OPIC emphasizes that sufficient equity contribution is an essential factor for a project's likelihood of success.

The financing plan should provide funds to meet all costs including feasibility studies, organizational expenses, land, construction, machinery, equipment, training and market development expenses, interest payments during construction, start-up expenses including initial losses, and adequate working capital.

The amount of OPIC's commitment varies. Factors considered are the degree that development in the host country benefits from the project, the project's financial requirements, and the extent that the financial risks and benefits are shared among the investors and the lenders. OPIC may assist in designing the financial plan and in coordinating it with other lenders and investors. In providing financing, OPIC can participate in up to fifty percent of the total costs of a new venture, while a somewhat higher participation may be considered in the case of an expansion of a successful existing business.

In recognition of possible cost overruns and early operating problems, and despite careful planning and allowance for contingencies in the financial plan, OPIC, like other limited recourse lenders, normally requires that the principal sponsors enter into an agreement under which they are obligated to guarantee payment of debt service to OPIC, as well as coverage of cost overruns prior to project completion. The definition of project completion includes certain financial and operating tests, as well as physical completion. The sponsors must have the financial capability to perform their obligations under this agreement.

For projects sponsored by U.S. small businesses or cooperatives, financing may be provided through direct loans. These loans generally range in amount from \$2 million to \$10 million. Loan guarantees, which typically are used for larger projects, generally range in size from \$10 million to \$100 million, but in certain instances can be as high as \$200 million. Under both financing techniques, the borrower first approaches the OPIC to analyze and structure financing for an overseas project. OPIC then determines the appropriate terms of borrowing. Where a guaranty is sought rather than a direct loan, the OPIC may assist in identifying a financial institution who would be willing to provide the needed funds. Guarantees are issued to U.S. financial institutions more than fifty percent beneficially owned by U.S. citizens, corporations, or partnerships. Foreign corporations that are at least ninety-five percent U.S. owned are also eligible, as are other foreign entities that are 100 percent U.S. owned. Typical funding institutions include insurance companies, pension funds, and commercial banks. These lenders are fully protected by the full faith and credit of the United States of America. OPIC-guaranteed loans are classified as eligible U.S. Government securities for insurance companies and other institutional investors. As a result, funding is available through fixed or floating interest rate obligations at approximately the same rates as those obtained by other U.S. Government agencies.

The repayment schedule of a direct or guaranteed loan will reflect the purpose of the loan and the projected level of cash flows to be generated by the project, which must be sufficient to meet interest and principal payments and to provide for an adequate return to equity investors. The terms of such loans, therefore, will typically provide for a final maturity of five to fifteen years following a suitable grace period during which only interest is payable. Interest rates on OPIC loans will vary with OPIC's assessment of the financial and political risks involved. They will also reflect interest rates in long-term capital markets in the United States. Interest rates on guaranteed loans are comparable to those of other U.S. Government-guaranteed issues of similar maturity and are subject to OPIC approval. For loan guaranties, OPIC charges the borrower a guaranty fee, which typically averages two and one-half to five percent per annum on the outstanding principal amount, depending upon commercial and political risk. In certain cases, OPIC will adjust its guarantee fee to include an income-sharing provision.

In general, OPIC expects that its creditor participation will be on a senior basis, *pari passu* with the holders of other senior debt, and that it will share in a first lien on fixed assets and any other appropriate collateral. A host government guarantee normally is not required by OPIC. Consistent with commercial lending practices, up-front, commitment, and cancellation fees are charged, and reimbursement is required for related out-of-pocket expenses, including fees for outside counsel and for the services of experts or consultants.

The proceeds of OPIC financing may be spent for capital goods and services in the United States, the host country, or other less developed countries.

OPIC's project financing is designed to complement and supplement the lending and investing facilities of commercial banks; local, regional and international development banks and investment funds; other agencies of the U.S. Government such as the Export-Import Bank of the United States; and a number of other multilateral lending institutions including the World Bank, the International Finance Corporation, the European Bank for Reconstruction and Development, and the Asian Development Bank. OPIC advises and assists U.S. sponsors in securing debt and equity financing from these institutions where appropriate in conjunction with OPIC financing. Many of OPIC's financings involve at least one other lender or independent investor, and in large projects several such institutions are typically involved. OPIC's willingness to finance a substantial portion of debt requirements, to accept longer or more flexible maturities, and to finance at fixed interest rates may facilitate participation of other lenders and investors in a project.

b. Support of Private Investment Funds.

Often, U.S. companies cannot allocate or raise sufficient equity capital to start or expand their businesses overseas. This may lead a company to place excessive reliance on debt financing; reliance on debt is generally inadvisable in those economically volatile countries where the business infrastructure is unreliable. OPIC, therefore, has provided financing to support a number of privately owned and managed direct investment funds that have the capability to provide equity capital to facilitate business formation and expansion.

Typically, OPIC-supported investment funds invest in five to forty percent of the equity capital of each of their portfolio companies and own interests in ten to twenty companies when fully invested. Some of the funds invest primarily in smaller companies, while others invest primarily in larger projects. Each portfolio company must have a significant business connection with the U.S. economy, and must meet OPIC's standards with respect to impacts on U.S. employment, the environment, and worker rights. The fund manager typically is a voting member of each portfolio company's board of directors or other governing body. The manager is also active in guiding the portfolio company, particularly in strategic planning and maintaining effective access to capital markets needed for business growth. The investment funds are privately owned, privately managed, and make their own commercially based investment decisions.

c. Political Risk Insurance.

OPIC provides political risk insurance to U.S. investors, contractors, exporters, and financial institutions involved in international transactions. Insurance is available for investments in new ventures or expansions of existing enterprises and can cover equity investments, parent company and third party loans and loan guaranties, technical assistance agreements, cross-border leases, assigned inventory or equipment, and other forms of investment. Coverage is also available for contractors' and exporters' exposures, including unresolved contractual disputes; wrongful calling of bid; performance; advance payment and other guaranties posted in favor of foreign buyers; and other risks. OPIC covers the same types of risks that the Ex-Im Bank political risk policies cover: currency convertibility and the inability to transfer funds due to changes in the host country's economic policies, and risks of loss due to political violence, including expropriation.

4. *Small Business Administration.*

To assist small businesses with their export financing needs, the Small Business Administration (SBA), Office of International Trade has developed several programs.

a. *Loan Programs.*

(i) *Export Working Capital Program.*

The first program available is the Export Working Capital Program (EWCP), a program developed through the combined efforts of the SBA and the Export-Import Bank.⁴⁰ The EWCP is a program that provides short-term working capital loans for the purpose of financing export transactions.⁴¹ The loans are transaction-specific and are for amounts of \$833,333 or less.⁴² Loan maturities may be for up to three years with annual renewals.⁴³ Exporters may use the proceeds from this program for the following: "(a) [t]o acquire inventory; (b) [t]o pay the manufacturing costs of goods for export; (c) [t]o purchase goods or services for export; (d) [t]o support standby letters of credit; (e) [f]or pre-shipment working capital; and (f) [f]or post-shipment foreign accounts receivable financing."⁴⁴ The EWCP provides repayment guarantees of ninety percent to commercial lenders

40. See generally the SBA's web-site (visited Feb. 17, 1998) <<http://www.sbaonline.sba.gov/OIT/finance/ewcp.html>>.

41. 13 C.F.R. § 120.340 (1997). "Loans can be for single or multiple export transactions. An export transaction is the production and payment associated with a sale of goods or services to a foreign buyer." *Id.*

42. See generally the SBA's web-site at (visited Feb. 17, 1998) <<http://www.sbaonline.sba.gov/OIT/finance/ewcp.html>>.

Loan requests of \$833,333 or less are processed by the SBA while loan requests over \$833,333 are to be processed through the Export-Import Bank. Borrowers may also have other current SBA guaranties, as long as the SBA's exposure does not exceed \$750,000. When an EWCP loan is combined with an international trade loan, the SBA's exposure can go up to \$1.25 million. *Id.*

43. 13 C.F.R. § 120.340 (1997).

44. 13 C.F.R. § 120.342 (1997). There are certain other limitations regarding the use of SBA financing. For example, SBA loans cannot be used for the following: to finance floor plan needs; to purchase real estate where the participant has issued a forward commitment to the builder/developer, or where the real estate will be held primarily for investment purposes; to make payments to owners or pay delinquent withholding taxes; to pay existing debt unless it can be shown that the refinancing will benefit the small business and that the need to refinance is not indicative of imprudent management (proceeds can never be used to reduce the exposure of the participant in the loans being refinanced) (visited Feb. 17, 1998) <<http://www.sbaonline.sba.gov/OIT/finance/ewcp.html>>.

and offers exporters preliminary commitments that encourage lenders to provide credit. To be eligible, the small business concern must have been in operation, though not necessarily exporting, for at least twelve months.⁴⁵

(ii) *International Trade Loan Program.*

The International Trade Loan Program (ITL) provides medium- to long-term (up to twenty-five years) working capital loans. This program is designed to help small businesses that are engaged or preparing to engage in international trade, as well as small businesses adversely affected by competition from imports.⁴⁶ Loans are made by lending institutions with the SBA guaranteeing a portion of the loan; the SBA can guarantee up to \$1.25 million to the borrower.⁴⁷ The applicant must establish either that the loan proceeds will significantly expand existing export markets or develop new export markets, or that the small business is adversely affected by import competition. In addition to these two requirements, the applicant must establish that upgrading facilities or equipment will improve the applicant's competitive position.⁴⁸ Proceeds may be used for working capital and/or facilities or equipment.⁴⁹ Maturities of loans for facilities or equipment are eligible for the twenty-five year maximum term. The applicant must have a business plan reasonably supporting its projected export sales.⁵⁰

b. *General Terms of SBA Financing.*

Interest rates and fees are negotiable between the lender and the small business exporter. SBA loan programs are generally intended to encourage longer term small business financing, but actual loan maturities are based on the ability to repay, the purpose of the loan proceeds, and the useful life of the assets financed. Regardless of the specifics of a particular transaction, however, maximum loan maturities have been established: twenty-five years for real estate and equipment; and, generally seven years for working capital. Loans for working capital purposes will not exceed seven years, except when a longer maturity (up to ten years) may be needed to ensure repayment. The maximum maturity of loans used to finance fixed assets other than real estate will be limited to the economic life of those assets, but in no event to exceed twenty-five years. The twenty-five year maximum will generally apply to the acquisition of land and buildings or the refinancing of debt

45. Eligibility requirements are detailed more extensively at the SBA's web-page. *Id.* In addition, for a definition of "small business" for purposes of the Small Business Administration, see 13 C.F.R. § 121 (1997) *et seq.* The "SBA may waive [the one-year] requirement if the applicant has sufficient export trade experience or other managerial experience." 13 C.F.R. § 120.341 (1997).

46. 13 C.F.R. § 120.345 (1997).

47. 13 C.F.R. § 120.348 (1997). The "SBA can guarantee up to \$1,250,000 for a combination of fixed-asset financing and working capital, supplies and EWCP assistance. The fixed-asset portion of the loan cannot exceed \$1,000,000 and the non-fixed asset portion cannot exceed \$750,000." *Id.*

48. 13 C.F.R. § 120.346 (1997).

49. "The Borrower may use loan proceeds to acquire, construct, renovate, modernize, improve, or expand facilities and equipment to be used in the United States to produce goods or services involved in international trade, and to develop and penetrate foreign markets." 13 C.F.R. § 120.347 (1997).

50. 13 C.F.R. § 120.345 (1997).

incurred in their acquisition. Where business premises are to be constructed or significantly renovated, the twenty-five year maximum would be in addition to the time needed to complete construction (significant renovation means construction of at least one-third of the current value of the property).

Interest rates are negotiated between the borrower and the lender, but are subject to SBA maximums, that are pegged to the Prime Rate.⁵¹ The only time a commitment fee may be charged is for a loan made under the Export Working Capital Loan Program. Interest rates may be fixed or variable. Fixed rate loans must not exceed Prime Plus two and one-quarter percent if the maturity is less than seven years, and Prime Plus two and three-quarters percent if the maturity is seven years or more. For loans of less than \$25,000, the maximum interest rate must not exceed Prime Plus four and one-quarter percent and four and three-quarters percent, respectively; for loans between \$25,000 and \$50,000, maximum rates must not exceed three and one-quarter percent and three and three-quarters percent, respectively. Variable rate loans may be pegged to either the lowest prime rate or the SBA optional peg rate. The optional peg rate is a weighted average of rates the federal government pays for loans with maturities similar to the average SBA loan. It is calculated quarterly and published in the Federal Register. The lender and the borrower negotiate the amount of the spread which will be added to the base rate. An adjustment period is selected that will identify the frequency at which the note rate will change. It must be no more often than monthly and must be consistent (e.g., monthly, quarterly, semiannually, annually or any other defined, consistent period).

To offset the costs of the SBA's loan programs to the taxpayer, the Agency charges lenders a guaranty and a servicing fee for each loan approved. These fees can be passed on to the borrower once they have been paid by the lender. The amount of the fees are determined by the amount of the loan guaranty. When the guaranty portion of the loan is \$80,000 or less, the guaranty fee will be two percent of the guaranteed portion; for loans more than \$80,000 but less than \$250,000, a three percent guaranty fee will be charged; for the next \$250,000 of the guaranteed portion, a 3.5 percent guaranty fee will be charged; for any portion greater than \$500,000, a 3.875 percent guaranty fee will be charged. In addition, all loans will be subject to a fifty basis point (0.5%) annualized servicing fee, which is applied to the outstanding balance of SBA's guaranted portion of the loan.

For those applicants that meet the SBA's credit and eligibility standards, the Agency can guaranty up to eighty percent of loans of \$100,000 and less, and up to seventy-five percent of loans above \$100,000 (generally up to a maximum guaranty amount of \$750,000).

A borrower must give SBA a first security interest equal to 100% of the EWCP loan amount (such as insured accounts receivable or letters of credit) or the guaranty amount.⁵² Collateral must be located in the United States, its territories or possessions.⁵³

51. The "SBA does not prescribe the interest rates for the EWCP, but will monitor these rates for reasonableness." 13 C.F.R. § 120.344 (1997).

52. 13 C.F.R. § 120.343 (1997).

53. *Id.*

5. *Commodity Credit Corporation.*

The United States Department of Agriculture's (USDA) Commodity Credit Corporation (CCC) administers export credit guarantee programs established to ensure financing for sales of U.S. agricultural commodities overseas.⁵⁴ The Export Credit Guarantee Program (GSM-102) provides coverage for financing with repayment terms from ninety days to three years. The Intermediate Export Credit Guarantee Program (GSM-103) provides coverage on credit terms longer than three years to ten years. Currently, maximum terms under GSM-103 do not exceed seven years.

Through these programs, the USDA makes about \$5.5 billion in coverage available globally each fiscal year. The purpose of these programs is to allow foreign buyers to purchase U.S. agricultural commodities from private U.S. exporters, with U.S. banks providing financing to the importers' banks on commercial terms. Under both programs, CCC is the guarantor and does not finance the export of the commodities. CCC typically insures up to ninety-eight percent of the principal and a portion of the interest. Both guarantee programs provide variable interest rate coverage, which is based on a percentage of the average investment rate of the fifty-two week treasury bill. These programs operate in countries where credit is necessary to increase or maintain U.S. exports and where private financial institutions may be unwilling to provide financing without the CCC's guarantee and assist overseas buyers in making commercial purchases.⁵⁵

An exporter must qualify under the credit programs before applying for a guarantee. In order to qualify, the exporter must have a business office in the United States and not be debarred or suspended from participating in CCC programs. The exporter must also submit documentation outlined in the regulations to start the qualifying process. Once the exporter has qualified, it is his or her responsibility to negotiate the sale. CCC is solely the guarantor under this program.⁵⁶ It is the responsibility of the exporters and importers to determine the commodity specifications and work closely with banks involved in arranging the credit terms associated with the sale. Any discounts and allowances will be excluded from coverage. Once a firm sale exists, the qualified exporter may apply for payment guarantee to cover the sale. An exporter must apply for the coverage prior to export.

Applications are processed on a first-come, first-served basis. If the application is approved, USDA issues a payment guarantee to the U.S. exporter. The exporter typically assigns right-to-proceeds, which may become payable under the guarantee to a U.S. bank that arranges to extend credit to the eligible foreign bank. USDA charges a fee for its guarantees, which is paid by the exporter and calculated on the basis of guaranteed value.⁵⁷

54. See the U.S. Department of Agriculture's web-page at <<http://www.usda.gov>> (visited Jan. 10, 1998). See also 7 C.F.R. § 1493 (1997) *et seq.*, for regulations governing the Commodity Credit Corporation.

55. See 7 C.F.R. § 1493.4 - 1493.6 (1997) (discussing criteria for country allocations). See also 7 C.F.R. § 1493.10 (1997).

56. 7 C.F.R. § 1493.70 (1997). "The payment guarantee fee rates will be based upon the length of the payment terms provided for in the export sale contract, the degree of risk that CCC assumes, as determined by CCC, and any other factors which CCC determines appropriate for consideration. A current schedule of the guarantee fee rates charged by CCC under GSM-102 and GSM-103 will be available upon request from the . . . USDA." *Id.*

57. See 7 C.F.R. § 1493.10(b) (1997).

Guarantee fees are not bank fees and they are non-refundable. Once the eligible financial institutions are established, a dollar denominated, irrevocable letter of credit (L/C) must be opened in favor of the exporter by an approved foreign bank.⁵⁸ Such L/Cs are ordinarily advised or confirmed through a U.S. bank selected by the foreign bank. The exporter must provide a written report within sixty calendar days if the export was made by rail or truck; or thirty calendar days if the export was made by any other carrier. Once the U.S. exporter delivers the commodities under the terms specified in the sales contract, documents required under the L/C and payment guarantee are submitted to the U.S. bank for payment.⁵⁹

B. UNITED STATES PRIVATE SECTOR OPTIONS.

1. U.S. Department of Commerce Trade Information Center.

Despite the legion government export financing programs, some exporting firms' financing needs can only be met in the private sector. Indeed, by their charters, U.S. Governmental agencies cannot compete with private sources of financing if those sources are available to the exporter. The U.S. Department of Commerce Trade Information Center has assembled a list of alternative financing programs to inform U.S. businesses of the types of financial services available from private businesses.⁶⁰ This list is quite extensive, and should be a good starting point for any exporter seeking to gain a better perspective on the private sector financing options available to her.

2. Access to Capital Program.

The Banker's Association for Foreign Trade is a trade association whose members are domestic and international banks who provide financing for trade transactions. This Association has created the Access to Capital Program (AXCAP) that essentially is a database that provides a listing of banks offering trade finance, projects of interest to exporters and banks, and services offered by government credit support agencies.⁶¹

3. Private Export Funding Corporation.

The Private Export Funding Corporation (PEFCO) finances the purchase of U.S. exports by providing medium- and long-term fixed interest rate loans to foreign importers. PEFCO is owned by thirty-five commercial banks, seven industrial companies, and three financial service companies. The interest and principal of PEFCO loans is guaranteed by Ex-Im Bank.⁶²

58. *Id.*

59. *Id.*

60. See the U.S. Department of Commerce's International Trade Administration's web-site (visited Jan. 7, 1998) <<http://www.ita.doc.gov>>. The alternative financing guide "was assembled by the Trade Information Center, Office of Export Promotion Coordination, U.S. Department of Commerce, HCHB 7242, Washington D.C. 20230. [The TIC] can be contacted at (800) USA-TRADE." See ITA's web-page (visited Jan. 7, 1998) <http://www.ita.doc.gov/how_to_export/finance.html>.

61. See WIEGLEY, *supra* note 2, at VI-10. Contact the Bankers' Association for Foreign Trade at 1600 M Street, N.W., Suite 7F, Washington, DC 20036, telephone # (202) 452-0013, fax # (202) 452-0959.

62. See WIEGLEY, *supra* note 2, at V-97, for a more detailed discussion of PEFCO's programs.

IV. Canada.

A. INTRODUCTION.

Exporting is extremely important to the Canadian economy as export transactions now account for forty-one percent of Canadian GDP and two out of every five jobs.⁶³ Canada's economy has not suffered too severely from the recent Asian debt crisis, as eighty percent of Canada's exports go to the United States, whose economy has remained strong despite Asia's woes.⁶⁴ Nevertheless, as thirty percent of Canada's exports are in raw materials, declining world commodity prices, caused by lower Asian demand, will undoubtedly effect Canada's economy.⁶⁵ Because of Canada's heavy reliance on exports, the price of the Canadian dollar is a significant indicator of the health of the Canadian economy.⁶⁶ While the value of the "loonie" fell to an all time low in February 1998, the Bank of Canada has raised interest rates to stop its slide.⁶⁷ Despite the weak performance of the Canadian dollar, Bank of Canada Governor Gordon Thiessen has pointed out that "the important factor for Canadian business is that long-term interest rates remain low on a sustainable basis" and the fact that "long term rates remain low reflects the confidence of foreign investors in Canadian assets."⁶⁸

Judging by the extent and number of export financing options the Canadian Government has made available, Canada assuredly recognizes the important role exporting plays in its economy. At the very least, a lack of financing options available to Canadian businesses will not be a cause of any future decrease in the Canadian exporting sector.

B. EXPORT FINANCING OPTIONS PROVIDED BY CANADIAN GOVERNMENTAL ENTITIES.

1. *Canadian Export Development Corporation.*

In operation for more than fifty years, Canada's Export Development Corporation (EDC) is a financial services corporation owned by the Government of Canada. It is dedicated to helping Canadian businesses compete in world markets.⁶⁹ The overall goal of the

63. Graham Clayton, *When private sector funding dries up*, NORTHERN ONTARIO BUS., June 1, 1997, available in 1997 WL 9087470.

64. Scott Morrison, *Canada's Central Bank Chief Talks up Dollar*, FIN. TIMES, Feb. 7, 1998, at 3, available in 1998 WL 3530956. Bank of Canada Governor Gordon Thiessen said that the impact of the Asian debt crisis on Canada should be "relatively modest" because Canada's trade with Asia accounts for less than 10% of its total exports. *Canada's Thiessen Outlook—1998 Growth Seen Less Robust*, DOW JONES NEWS SERVICE, Feb. 5, 1998.

65. Patrick Bloomfield, *Ripples From Asia Still to Reach These Shores*, THE FIN. POST, Jan. 31, 1998, at 40, available in 1998 WL 7190399.

66. *Canada's Thiessen Must Keep Eye on Monetary Conditions*, DOW JONES NEWS SERVICE, Feb. 5, 1998.

67. *Id.*

68. *Id.*

69. Much of the discussion regarding the EDC and its programs comes verbatim from the EDC's web-pages, and in particular (visited Feb. 17, 1998) <<http://www.edc.ca/english/info/99-02inf.html>>. For more information, contact the EDC at 151 O'Connor Street, Ottawa, Canada, K1A 1K3, phone: (888) 332 - 3320, e-mail address: export@edc4.edc.ca. See generally the EDC's statutory enactment, the Export Development Act, R.S.C. 1985, ch. E-20 *et seq.* (1997).

EDC is to help Canadian exporters cultivate "long-term partnerships with [their] global buyers."⁷⁰ The EDC is financially self-sustaining, operates on commercial principles, and does not provide subsidies to businesses.⁷¹ The Corporation is governed by a board of directors composed of representatives from both the private and public sectors, and reports to the Canadian Parliament through the Minister for International Trade.⁷²

The Canadian Parliament passed legislation in 1993 to modernize the capabilities of the EDC. The changes and related regulations (passed in 1994) gave the EDC more flexible and comprehensive powers for the assistance of Canadian businesses in their international endeavors.⁷³ In 1996, of the EDC's 2,965 customers, 2,520 are small- to medium-sized businesses. At the close of 1997, the EDC had 3,100 customers.⁷⁴ Total business volume of the EDC in 1996 was C\$22 billion, up twenty-eight percent over 1995.⁷⁵ In 1996, shareholder equity totaled C\$1.4 billion, and net income was C\$112 million.⁷⁶ In 1997, income was C\$128 million.⁷⁷ The EDC earned \$66 million in the first half of 1997, which was an increase of \$6 million over the same period in 1996.⁷⁸

The EDC's assets totaled \$11.7 billion at the end of November 1997.⁷⁹ Its portfolio has changed dramatically over the last decade; ten years ago, most of the EDC's export credit was "sovereign risk" loans to foreign states and their nationalized companies. Now, while some of their assets still fall into the same category, most of the EDC's loans are commercial in nature. More than any other reason, worldwide privatization is the cause for this shift.⁸⁰

The EDC is specifically aiming its export financing programs toward Latin America. The EDC cites the following as reasons for Latin America's attractiveness: a market of 450 million people; rich untapped natural resources; increasing political stability on a region-wide basis; fast growing economies; open markets; balanced budgets; privatization of state-owned companies; reduced tariffs; improvements in manufacturing facilities; and infrastructure upgrades. Canada's exports to the region of Latin America exceeded US\$4.5 billion in 1995, making Latin America Canada's fifth-largest export market. Canadian direct investment in Latin America since 1990 has increased by more than 190%, to US\$7.6 billion in 1995.⁸¹ With the NAFTA ratified in 1994 and a bilateral Free Trade Agreement with Chile ratified in November of 1996, the EDC specifically wants to facilitate Canadian

70. EDC web-page (visited Feb. 17, 1998) <http://www.edc.ca/english/risk/general_product/99-03.html>.

71. *Id.* at <<http://www.edc.ca/english/info/99-02inf.html>>. For arguments for and against the EDC's profit-making ability, see *Export Finance, Canada's Export Finance Clash*, PROJECT & TRADE FIN., Nov. 1, 1996, at 36, available in 1996 WL 16220113. See also Gordon, *supra* note 33.

72. EDC web-page (visited Feb. 17, 1998) <http://www.edc.ca/english/risk/general_product/99-03.html>.

73. *Id.* at <http://www.edc.ca/english/risk/general_product/99-87.html>.

74. *Id.*

75. *Id.*

76. EDC, *supra* note 69, at <<http://www.edc.ca/english/info/99-02inf.html>>.

77. *Canada's Export Development Corp. Says Business Volume Up 30% in 1997*, DOW JONES NEWS SERVICE, Feb. 5, 1998.

78. Gordon, *supra* note 33.

79. *Id.*

80. *Id.*

81. EDC, *supra* note 69, at <<http://www.edc.ca/english/info/winter97/el9.html>>.

exporting firms' increased access to the world's largest open-market.⁸² In 1996 the EDC supported more than US\$82 million worth of exports to Latin America.⁸³ Looking forward, the EDC predicts that Latin America will represent a US\$2 trillion economy trading more than US\$600 billion in goods and services by the year 2000.

a. EDC Programs.

Generally, the EDC provides a wide range of financial and risk management services, including export credit insurance, a broad range of export financing including financing to foreign buyers of Canadian goods and services, political risk insurance, and loan guarantees.⁸⁴ The Corporation delivers its products and services through eight sector-based customer teams plus a cross-sector team dedicated to serving smaller exporters, supported by a network of centers of expertise that provide in-depth knowledge, research, analysis, and skills. The EDC has the capability of structuring its financing to include repayment terms that correspond to the life of a financed asset. The EDC also has access to important information regarding geographic and product markets around the world. These industries include aerospace, machine, transportation, telecommunications, and business services. Information regarding these markets is critical for accurate risk analysis.⁸⁵

(i) *Export Financing Options.*

The Canadian Export Development Corporation provides several different types of export financing programs. These financing options provided by the EDC fall into three broad categories: supplier credit financing, buyer credit financing, and protocols.

(A) *Supplier Credit Financing.*

The EDC's Supplier Credit Financing Program is primarily tailored for small- and medium-sized transactions.⁸⁶ The EDC accomplishes its Supplier Credit Financing through a note purchase agreement with the Canadian exporter.⁸⁷ Through the note purchase agreement, the EDC purchases from an exporter a series of promissory notes issued by a foreign buyer to the exporter upon the sale of goods or services.⁸⁸ Once the customer receives the product, the EDC then pays the Canadian exporter, in a manner similar to financing under a letter of credit.

(B) *Buyer Credit Financing.*

(I) *Direct Buyer Financing.*

The EDC will extend credit directly to a foreign purchaser of a Canadian exporter's goods. Buyer credit financing includes direct loans and lines of credit arranged between

82. *Id.*

83. *Id.*

84. *Id.* at <<http://www.edc.ca/english/info/99-02inf.html>>.

85. *Id.* at <http://www.edc.ca/english/risk/general_product/99-04.html>.

86. *Id.* at <http://www.edc.ca/english/risk/financing_product/loc-eng.html>.

87. *Id.*

88. *Id.*

the EDC and the buyer, or a borrower on behalf of a buyer, for a set transaction.⁸⁹ These loans normally are for larger amounts and have longer repayment terms.⁹⁰

(II) *Lines of Credit.*

The EDC line of credit is an arrangement whereby the EDC lends money to a foreign bank, institution, or purchaser, which in turn lends the necessary funds to foreign purchasers of Canadian goods and services. The lines of credit are designed for use by a foreign purchaser who is unable to secure financing for an import purchase from a domestic bank. The program is designed to support sales to the mid-market. Interest rates, repayment terms, and other terms of the agreement are pre-arranged between the EDC and the foreign borrower, thus speeding up turn-around time once the underlying agreement has been negotiated. Line of credit transactions typically range between US\$50,000 and US\$5 million. In 1997 the EDC had forty-seven total lines of credit outstanding, and these lines provided financing for buyers in twenty-two countries.⁹¹

The typical procedure for underwriting a line of credit is as follows. The exporter and buyer first negotiate the underlying transaction. The EDC will have already extended a line of credit to a local bank, and the buyer begins the process for obtaining EDC financing. The exporter submits a preliminary application for financing to the EDC, along with a Canadian Content Report. The exporter also obtains an exposure fee quote and an indication of any other costs. The buyer will likely ask the exporter to obtain a written commitment from the EDC that it is willing to consider financing the transaction. This commitment is contained in a management letter (letter of interest) issued by the EDC provided that its lending criteria are met. These criteria include approval of the exporter's goods and its financial and technical capacity to undertake the project. Complete details of the underlying transaction are forwarded to the EDC, including a copy of the draft commercial contract or purchase order. If the exporter is approved, a commercial contract is signed and the local bank submits a financing request to the EDC. Provided that the EDC's financing criteria are still met at this point in the transaction, the EDC funds the loan. Once funding has been obtained, the EDC advises the bank to forward a Disbursement Order to EDC. The Disbursement Order authorizes the EDC to disburse funds to the exporter based upon the payment terms contained in the commercial contract. The EDC then forwards the Disbursement Order to the exporter. The exporter provides the EDC with the documentation required by the Disbursement Order. This documentation usually consists of invoices and shipping documents, as well as confirmation that the exporter has received the fifteen percent cash down payment from the buyer. At that point the EDC disburses funds to the exporter.⁹²

(C) *Protocols.*

Protocols are agreements between the EDC and a foreign financial institution by which the EDC agrees to consider, on an individualized basis, guarantees that the foreign institution extends to EDC's financing of subsequent transactions.

89. *Id.*

90. *Id.*

91. *Id.* See also *Id.* at <<http://www.edc.ca/english/info/winter97/e05.html>>.

92. *Id.* at <<http://www.edc.ca/english/info/winter97/e05.html>>.

(ii) *Other Financing Options.*

(A) *Leasing.*

The EDC also acts as a lessor/owner in a capital lease financing transaction. This type of arrangement is available when normal loan arrangements are not practicable and/or where the buyer prefers a lease over a loan. The EDC will evaluate the lessee's creditworthiness just as it would any other borrower under a direct lending program.

(B) *Pre-Shipment Financing.*

Pre-shipment financing is a facility that allows exporters to meet pre-shipment financing requirements by making EDC financing available directly to Canadian companies to cover specific up-front capital costs related to a long-term export contract.

(C) *Masters Accounts Receivable Guarantee Program.*

Pursuant to EDC's Master Accounts Receivable Guarantee (MARG) program, banks can extend credit to an exporter using the exporter's accounts receivables as collateral. The EDC guarantees ninety percent of the loan amount if the exporting firm becomes insolvent.⁹³

(iii) *CIBC/EDC Grow Export Program.*

One specialized industry that the EDC is trying to serve is Canada's "knowledge-based" industry. The EDC defines as "knowledge-based" a business enterprise that has as its primary "business objective the development, marketing and manufacture of a technologically advanced product or service and is depending primarily for its success on the application of technology through its own research or research acquired by others."⁹⁴ Examples of knowledge-based businesses include high-tech firms, bio-technology, information technology, and computer software manufacturing firms.⁹⁵ Knowledge-based industries are currently the fastest growing segment of the Canadian economy.⁹⁶ Nevertheless, lenders are faced with unique challenges when attempting to provide financing for knowledge-based firms.

Knowledge-based firms have several characteristics that make lenders nervous. Unlike traditional industries, knowledge-based firms are more strongly driven by exports. Knowledge-based industries are also different from traditional manufacturing firms in that knowledge-based industries usually have different capital structures than traditional manufacturing. In the past, financial institutions "have been uncomfortable with the lack of 'hard' assets such as buildings or machinery, with which to secure loans and lines of credit . . . Pre-shipment working capital required [of a knowledge-based industry] to perform under an export contract, including additional unknown variables, simply tends to increase risk and further tighten credit availability," states EDC's Information Technologies Team Leader, Peter Foran.⁹⁷

93. *Id.* at <<http://www.edc.ca/english/info/winter97/e09.html>>.

94. *Id.* at <<http://www.edc.ca/english/info/winter97/e08.html>>.

95. *Id.*

96. *Id.*

97. *Id.*

To specifically meet the needs of Canada's knowledge-based exporting firms, the EDC has developed the CIBC/EDC Grow Export program and knowledge-based industries guarantee.⁹⁸ This program is a "50/50 shared risk program that supports working capital loans made by CIBC for small- and medium-sized enterprises (SMEs)⁹⁹ in knowledge-based industries in support of firm contracts."¹⁰⁰ The financing made available through the CIBC would provide for a one-time draw of up to ninety percent of the hard costs of the export contract. EDC provides a guarantee for fifty percent of the loan amount made to SMEs in this industry.

(iv) *Agri-Food Credit Facility.*¹⁰¹

The Agri-Food Credit Facility (ACF) was announced in February 1995 in order to enhance existing government guaranteed credit programs. Its purpose is to enable Canadian exporters to better meet competition from other exporting country's export credit programs.¹⁰² The ACF is intended to be used as a last resort and to match credit terms provided by foreign competitors. It is administered by the EDC on behalf of Agriculture and Agri-Food Canada. The ACF is available to all Canadian agriculture and agri-food exporters under appropriate circumstances.

The ACF can support up to \$1 billion in additional credit or credit insurance for export sales to non-sovereign foreign buyers. The ACF allocates support as follows: \$700 million is for Canadian Wheat Board (CWB) wheat and barley; \$200 million for all other agri-food products and commodities; and \$100 million currently unallocated but to be directed as market demand dictates. This allocation was based on historical and future anticipated use of export credit for agri-food products recognizing that export credit from all exporters is primarily used on grains. For non-CWB commodities, the ACF will be available where the business cannot be covered by the EDC's credit insurance programs.¹⁰³

98. From the Canadian Imperial Bank of Commerce web-site: The "CIBC is a diversified group of financial services companies based in Canada and operating on a global basis. With roots dating back to 1867, we have grown to become Canada's second largest Financial Institution and one of the 10 largest banks in North America. Our group of companies today has more than \$227 billion (Canadian) in assets and a capital base of more than \$12 billion. In fiscal 1996, our 40,000 employees helped us achieve a net income exceeding \$1.366 billion. CBC and its subsidiaries comprise Personal and Commercial Bank and CIBC Wood Gundy. Personal and Commercial Bank provides a full range of financial services to several million individuals and businesses across Canada." CIBC (visited Nov. 15, 1997) <<http://www.cibc.com/inside/>>. For a CIBC knowledge-based business representative, phone 1(800)551-0606. EDC, *supra* note 69, at <<http://www.edc.ca/english/info/winter97/e08.html>>.

99. "A[n] SME is defined as a company having annual sales of less than [C]\$25 million." EDC, *supra* note 69, at <<http://www.edc.ca/english/info/winter97/e08.html>>.

100. *Id.*

101. The discussion of the ACF program comes from the Canada Business Service Centres' (CBSC) web-page. CBSC (visited Apr. 7, 1998) <<http://www.cbcs.org/about.html>>.

102. See *supra* discussion of the United States' Commodity Credit Corporation (CCC), text accompanying notes 54-59.

103. See discussion *infra*, text accompanying notes 105-114.

For example, if the exposure limit for a particular country has been exceeded, but the transaction is deemed to be commercially viable, the ACF may be accessed.¹⁰⁴

d. EDC Insurance Capabilities.

Unique among government export financing agencies among the G7 countries, the EDC provides insurance and loan guarantees, along with direct lending programs.¹⁰⁵ The EDC insurance policies protect exporters against various losses due to commercial and political risks. Risk types include buyer insolvency, default on payments, repudiation of goods, contract termination, foreign exchange conversion or transfer payment difficulties, war, revolutionary insurrection preventing payment, cancellation of government import or export permits, wrongful calls on bid/performance letters of guarantee, and inability to repatriate capital or equipment due to political problems.¹⁰⁶ Specific EDC insurance services include: short- and medium-term credit insurance; bid/performance-related insurance and guarantees; surety bond support; equipment (political risk) insurance; and foreign investment insurance.

(i) *Foreign Investment Insurance.*

The first of the EDC's policies is the Foreign Investment Insurance (FII) policy. The FII can protect an exporter against up to ninety percent of its losses from investments abroad. The FII policy insures the exporter against losses due to three types of political risks. The first of these risks is the potential of financial loss due to the exporter's inability to transfer funds or convert foreign earnings into hard currency. The next is the risk of loss due to expropriation of assets directly by a foreign government or indirectly by a foreign person whose actions have been facilitated by a change in the foreign government's policies. The third type of risk is risk of loss due to politically motivated violence.

(A) *Terms.*

The EDC FII policy allows the exporter to choose coverage against any or all of the above-named risks. The FII policy gives the exporter up to fifteen years of coverage against political risks. The EDC provides coverage for the exporter's equity investment, plus

104. "Program information may be obtained at any of the AAFC offices across Canada or by calling the EDC at 1 (888) 332-5108. Provinces Eligible: Alberta; British Columbia; Manitoba; New Brunswick; Newfoundland; Northwest Territories; Nova Scotia; Ontario; Prince Edward Island; Quebec; Saskatchewan; Yukon." CBSC, *supra* note 101, at <<http://www.cbsc.org/fedbis/bis/2085.html>>.

105. *Canada, Export Finance, Canada's Export Finance Clash*, PROJECT & TRADE FIN., Nov. 1, 1996, at 36, 1996 WL 16220113. See also CBSC, *supra* note 101, at <<http://www.cbsc.org/manitoba/bis/1003.html>> (visited Jan. 12, 1998).

106. EDC, *supra* note 69, at <<http://www.edc.ca/english/info/99-02inf.html>>. Information regarding the EDC's export insurance options also comes from materials provided by the EDC to the author. The author would like to thank Mike Neals, Director of Marketing at the EDC for his assistance in obtaining this material. Contact the EDC at (613) 598-2500 or visit their internet sites listed in the other notes on the EDC financing options.

retained earnings coverage of up to an additional 200% of the equity investment. The EDC can cover any shareholder loan, plus interest on the loan of up to an additional 100%. The amount of coverage for other forms of investment will be based on the investor's actual exposure. The exporter can change the terms of coverage of its policy from year to year both to ensure full coverage against newly developing risks and to prevent unnecessary coverage for particular risks that are no longer present. To qualify for FII, the foreign investment must demonstrate benefits to both Canada and the host country.

(B) *Costs of Coverage.*

An annual premium is charged on the current amount of coverage for each risk covered. The amount of the premium varies, based on the host country and the industry. A nominal fee is charged on the difference between the maximum amount of coverage (the total amount of coverage available to the exporter) and the current amount of coverage (the amount of coverage in effect over the course of a year). Administration and due diligence fees reasonably incurred by EDC will be for the account of the policyholder.

(C) *Benefit.*

The primary benefit of this policy is that an exporter can more easily attract additional project capital as the investor is assured that its contribution is secured against losses due to political changes in the host country.

(ii) *Global Comprehensive Insurance.*

The EDC points out that accounts receivables can be one of the largest assets on an exporter's balance sheet, however, these are often overlooked when the exporter considers credit insurance. The Global Comprehensive Insurance policy can provide the following: protection against contract cancellation by an exporter's customer; insurance for Letters of Credit transactions on a country-by-country basis; inclusion of domestic receivables along with foreign receivables; coverage for sales made by foreign affiliates; invoicing in foreign currencies; and insurance for receivables generated by providing services. EDC's Global Comprehensive Insurance Policy is designed to protect a Canadian exporting firm's export accounts receivables. The policy covers up to ninety percent of losses resulting from a wide range of commercial and political risks. The EDC advertises this program as enabling the exporter to enter new markets and expand existing markets through the knowledge that credit extended through additional receivables is insured by the EDC. This program is also designed to improve the exporter's ability to secure working capital financing, and provides the exporter with access to EDC's Worldwide Credit Report Sourcing Facility. The exporter pays premiums for the Global Insurance Policy under a "pay as you go" plan, paying premiums to insure only goods the exporter actually exports. Premium rates are based on several factors, including: type of coverage selected; payment terms extended under the receivable; the type of goods being exported; and risks according to the buyer itself and the country in which the buyer is located. Since EDC's legislative mandate is to support Canadian business and therefore, the sale of Canadian goods and services, the EDC

requires that Canadian content of the exported goods or services be a minimum of fifty percent.¹⁰⁷ Presumably, waivers for this content requirement are available.¹⁰⁸

(iii) *Export Credit Insurance.*

EDC's Export Credit Insurance covers the exporter against ninety percent of losses if the foreign buyer does not pay for the goods received. Export contracts can be insured against a wide range of commercial and political risks including: bankruptcy of the foreign buyer; default by the foreign buyer; refusal of goods by the foreign buyer, provided that the exporter has met the contract terms; cancellation of contract before the exporter ships the goods (only when contract coverage is in place); payment delays caused by the prevention of funds transfers; war or hostilities in the buyer's country, or in other countries that affect the host country; and cancellation or non-renewal of export or import permits.

(A) *Requirements.*

The EDC indicates that the exporter can easily acquire this policy and applications can be processed over the phone. A requirement of the policy is that the exporter must insure all its exports sold on credit to all export markets unless the exporter has elected to exclude sales to the United States and/or all exports financed by Letters of Credit.

(B) *Benefits.*

Similar to the FII policy, this policy gives the exporter the benefit that because the receivables are insured by the EDC, a bank is more likely to accept the receivables as security when setting up an operating line of credit. This policy also allows the foreign buyers to pay for their goods over a longer period of time, and the exporter has added security knowing that the repayment is assured.

(iv) *Political Risk Insurance of Loans.*

Exporters investing and selling goods abroad expose both themselves and the banks involved in financing the transaction to political risks. The EDC's expanded Political Risk Insurance (PRI) builds on its Foreign Investment coverage for equity and other forms of investments with increased protection for loans. Lenders can be Canadian or non-Canadian. Eligible structures to access PRI include the following: loans to Canadian-sponsored projects; project loans involving non-Canadian investors, but where Canadian benefits will result; and loans for Canadian export sales unrelated to specific projects. PRI protects against the same three types of risks that the FII policy protects against (funds transfer problems, expropriation, and political violence) and is similar to the FII in that the exporter can decide which of these risks for which it will buy coverage. The EDC provides

107. EDC, *supra* note 69, at <http://www.edc.ca/english/risk/insurance_product/99-05.html>. "Therefore, the Canadian content should be a minimum of 50 percent, or other significant benefits to Canada should be achieved." *Id.* "The Corporation is established for the purposes of supporting and developing, directly or indirectly, Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities." Export Development Act, Interpretation, Purposes and Powers, R.S.C. 1985, c. E-20, s. 10(1) (1997).

108. EDC, *supra* note 69, at <http://www.edc.ca/english/risk/insurance_product/99-05.html>.

assistance to the exporter in identifying risks that the exporter will likely encounter in the countries in which it does business.

To qualify for PRI coverage, the transaction must demonstrate benefits to Canada. The transaction must involve risk sharing between the lender and the EDC. Ninety percent/ten percent co-insurance ratios are required with most insured parties, and to qualify for coverage, the loan must be to a non-sovereign borrower.

(v) *Insurance Coverage for Canadian Receivables.*

In addition to insurance for exporting receivables, recent Canadian legislative changes have enabled the EDC to provide receivables insurance for domestic accounts receivables. This extended service enables the firm doing business in Canada and abroad to insure against losses that could affect the firm's ability to remain in, or enter export markets. The EDC can provide this additional coverage by an endorsement to the exporter's current credits insurance policy.

With this domestic receivables program, a ninety percent/ten percent co-insurance ratio will apply for loss due to commercial risks. At its option, the firm can exclude from the policy sales to federal, provincial, and municipal governments. The business can assign the policy proceeds for domestic cover to its bank through a Direction to Pay or a Tri-Partite Agreement.¹⁰⁹

(vi) *Specific Transaction Insurance.*

In addition to the above named programs, the EDC also provides Specific Transaction Insurance. The Specific Transaction Insurance is similar in requirements and coverage to the above programs.¹¹⁰

The Specific Transaction Insurance guards against the previously named risks and also helps the exporter in other ways. The exporter can take advantage of new export opportunities because it knows that its exports are protected. The exporter is given the ability to be more competitive as it can offer more flexible payment terms to its customers. Claims proceeds can be assigned to the exporter's bank as collateral and thus the policy can enable the exporter to obtain additional working capital. The policy also protects the exporter's continued cash flow and corporate viability by timely assessment and payment of eligible claims for losses.

(vii) *Coverage for Contract Bonds.*

In conducting transactions abroad, exporters often must issue bonds and guarantees to their customers. These instruments cover the exporter's bid, his performance, and advances received from the customer. For most international transactions, this security is provided in the form of a bank Irrevocable Letter of Credit, also known as a Letter of Guarantee or Demand Guarantee. In North America, it is usually in the form of a bond issued on the exporter's behalf by a domestic surety company. Letters of Guarantee require the exporter's bank to pay on demand the amount stipulated, even in the absence of proof that the exporter has defaulted on the deal. When the guarantee could be for as much as

109. *Id.* at <http://www.edc.ca/english/risk/insurance_product/99-10.html>.

110. *Id.* at <http://www.edc.ca/english/risk/insurance_product/99-16.html>.

twenty-five percent of the project's total value, this puts the exporter's working capital or operating line of credit (provided as collateral against this guarantee) at risk. The EDC's Performance Security Insurance protects the exporter by covering ninety percent of the exporter's losses if the buyer makes a wrongful call or a call resulting from events outside of the exporter's control, such as war. This coverage can be extended to bid, advance payment, and performance guarantees.

A separate insurance policy, EDC's Performance Security Guarantee, provides the exporter's bank with 100% coverage against a call of a Letter of Guarantee issued on the exporter's behalf. The exporter's bank is fully covered against both wrongful and rightful calls. This policy normally allows the exporter to use the EDC's coverage as collateral, instead of requiring the exporter to commit its own resources.

Most North American buyers require the exporter to post Surety Bonds instead of bank Letters of Guarantee. EDC can assist in this process by insuring or re-insuring the bond issuer locally, guaranteeing the exporter's domestic bond company on international contracts; and in some instances, through issuance of the bond directly to the buyer.

Generally, the normal Canadian content requirements apply to the goods and services insured through these programs.¹¹¹ As criteria for approval, the EDC considers the exporter's managerial, technical, and financial capabilities. In addition, the EDC will require acceptable contractual terms and acceptable bonding and guarantee instruments. The EDC will consider the current conditions and economic outlook in the buyer's country and the history and current status of the buyer itself.¹¹²

(viii) *Documentary Credits Insurance.*

EDC's Documentary Credits Insurance Policy (DCIP) covers financial institutions confirming, negotiating, accepting, or paying Irrevocable Letters of Credit (ILCs) issued to exporters of Canadian goods and services. The DCI policy allows financial institutions to process ILCs in markets where they have a limited desire to enter, markets where the lender is unwilling to take the risk for their own account, or markets where financial institutions' credit lines are approaching or have reached country or foreign bank limits. In addition, with DCI protection, financial institutions may be willing to enter into inter-bank loan arrangements and refinance drawings under ILCs opened by foreign banks. The DCI insures the lender against non-payment by the foreign bank and thus enhances the lender's ability to provide confirmations and advance funds to the exporter. The DCI policy does not cover losses involving non-payment as a result of documentary disputes between the policyholder and foreign banks. These types of disputes must be resolved before a claim can be considered. Policies are held and administered by financial institutions.

(A) *Terms.*

Based on their internal credit guidelines, financial institutions will choose which transactions are submitted to the EDC for insurance. EDC will evaluate each request for coverage. Contingent upon the creditworthiness of the foreign bank in relation to the par-

111. See *supra*, text accompanying note 107.

112. Most of the discussion regarding the EDC's Coverage for Contract Bonds comes verbatim from the EDC, *supra* note 69, at <http://www.edc.ca/english/risk/insurance_product/99-17.html>.

ticular transaction, EDC will issue credit approval for the proposed transaction. Depending on the demand level, the EDC will establish national credit limits for foreign banks specializing in this type of financing. The DCIP insures the financial institution for ninety percent of the value of the ILC against the risk of non-payment by the opening bank. The coverage amount is upped to ninety-five percent in the case of exports of bulk agricultural goods. To access this program, a foreign bank opening ILCs on behalf of an importer of Canadian goods or services should contact an EDC Documentary Credits Insurance policyholder. The policyholder submits the transactions they want to insure, and each transaction is analyzed on an individual basis. If the transaction is acceptable, the EDC advises the policyholder by way of a credit approval for the specific transaction. No further exchange of information is necessary between the issuing bank and the EDC, provided that the EDC has up-to-date information regarding the issuing bank's current activities. Documentary credits must be issued subject to the Uniform Customs and Practices for Documentary Credits (UCP 500).¹¹³

ILC payments terms under the DCI policy can be: 180 days or less for exports such as raw materials, semi-manufactured products or consumers goods; as long as 360 days for other goods and services, including bulk agricultural commodities; more than 360 days for capital goods and services using medium-term coverage; or more than 360 days for bulk agricultural commodities, provided there is proof of officially supported competition warranting extended terms for the market and commodity in question (for this last term, coverage would be provided under the Medium-Term Bulk Agriculture Guarantee Program).

(B) *Benefits.*

The benefits of this policy are similar to the benefits the other EDC policies offer. In addition, the DCI allows the exporter to spend more time on business development while the bank as the policyholder handles most of the administrative work. The DCI improves cash flow possibilities as the bank may be prepared to discount ILCs knowing that payments are insured. Finally, the bank may be more predisposed to confirm ILCs the exporter receives from the foreign buyer's bank.¹¹⁴

113. Much of this discussion on the EDC's Documentary Credits Insurance comes verbatim from the EDC, *supra* note 69, at <http://www.edc.ca/english/risk/insurance_product/99-N.html>; See also International Chamber of Commerce, Uniform Customs and Practices for Documentary Credits (ICC Publication No. 500) (1994).

114. The terms include coverage for: ninety percent for most goods and services exports (with the exporter and policyholder usually determining how the uninsured portion will be shared); ninety-five percent for bulk agricultural commodities (with the exporter and policyholder usually determining how the uninsured portion will be shared) and in some instances, EDC may extend 100 percent protection for sovereign risk foreign banks; or for capital goods and services where terms of payment exceed 360 days, seventy-five percent or sixty percent of the amount financed by the policyholder (excluding a fifteen percent down payment) for non-OECD countries. The policyholder must take the uninsured portion of the risk themselves and the policyholder cannot take recourse against the exporter on the uninsured portion. *Id.* In order for an exporter to qualify for DCI coverage, goods and services for export must have a minimum of fifty percent Canadian content, or other significant benefits to Canada. Bulk agriculture exports must have: 100% Canadian content; be comprised of commodities which are crated for shipment in fresh, chilled, dried or frozen bulk containers, including products crated or boxed for shipment in

2. Other Canadian Government Agencies' Programs.

a. Canadian Commercial Corporation.

Citing the difficulty that SMEs experience in obtaining advance payment from customers on export sales, the Canadian Commercial Corporation (CCC) offers a program called the Progress Payment Program (PPP).¹¹⁵ To meet an exporter's working capital needs, through the PPP the CCC assesses the capabilities of the Canadian exporter and the risks associated with a particular exporting transaction. After assessing the exporter's capabilities and the merits of the transaction, CCC acts as a prime contractor for the deal. A participating bank provides funds for the export sale, beyond the company's normal line of credit, and once this line of credit is in place. As prime contractor, the CCC guarantees the exporter's contract performance by verifying the exporter's work done for the contract. The company accesses progress payments accordingly. The program is available to all firms with sales of \$50 million or less. Credit lines are limited to \$2 million per transaction, with no one company having more than \$2 million worth of exposure at any time.

Each application to this program carries a \$500 fee which is non-refundable; there is an additional charge of 1.5-2 percent over prime to cover CCC's indemnification risk. CCC also recovers its costs for contract administration and monitoring through a charge of 1-2 percent depending on the complexity of the deal.

b. Business Development Bank of Canada.

Formerly known as the Federal Business Development Bank (FBDB), the Business Development Bank of Canada (BDC) has recently started to provide financing for exporting that complements the services of the EDC.¹¹⁶ Its flagship export finance program is called "Working Capital for Exporters." Working Capital for Exporters is designed to help small businesses finance export and export-related activities. This product provides pre-shipment financing, of up to \$250,000, to cover the heavy costs associated with initiating and developing international markets. Flexible repayment terms allow small companies to build foreign sales and ensure the long-term viability of the exporter's company. This program allows a company to finance the following: an increase inventory; the costs involved with the production of finished goods; costs involved in increasing marketing and the development of distribution networks; and other development-related costs.

Generally, the exporter is only required to pay interest during the first year of the loan and subsequent payments may be based on projected cash flows. The financing carries a fixed or floating interest rate, and terms range from four to six years. To qualify for this

cargo holds (ship or air); and *not* combine two or more ingredients, be packaged in retail-sized packages, or include any forestry products or by-products. Documentary credits must be issued subject to the Uniform Customs and Practices (UCP) for Documentary Credits. *Id.*

115. See generally the Canadian Commercial Corporation, web-page (visited Jan. 12, 1998) <<http://www.ccc.ca/progress.htm>>.

116. This discussion of the Business Development Bank of Canada comes verbatim from its web-page <<http://www.bdc.ca/site/right/financ/index.html>>.

financing, the business must have in place the following: an existing line of credit with a chartered bank, credit union or *caisse populaire*; a normal level of working capital assistance from conventional sources; the business must have been in operation for at least two years; the exporter must have a solid management team; it must have a projected growth of export sales and good profit potential; the business must be currently exporting or is preparing to begin exporting; and the business must be prepared to work with BDC management and counselors.

In addition to the Working Capital for Exporters program, the BDC continues to offer its early growth "Microbusiness" program, "Working Capital for Growth" loans, and its "Patient" and "Venture" capital programs.

c. Program for Export Market Development.

The goal of the Program for Export Market Development (PEMD) is to finance marketing costs incurred by Canadian exporting business interests.¹¹⁷ Since its creation in 1971, the PEMD has assisted over 25,000 Canadian businesses in marketing their products and services abroad. Sales resulting from PEMD supported activities undertaken by the exporters exceed C\$11.5 billion. The emphasis of the PEMD is to "increase export sales of Canadian goods and services by sharing the costs of activities that companies normally could not or would not undertake alone, thereby reducing risks involved in entering a foreign market." The funding provided by the PEMD is a loan whose repayment schedule is based upon subsequent sales made by the exporting company and the number of contracts with foreign firms the exporter obtains.

Under the direction of the Export Programs Division (TCE) of the Department of Foreign Affairs and International Trade (DFAIT), and jointly administered with Industry Canada (IC), through the regional International Trade Centres, the PEMD has four major elements: (1) Market Development Strategies (MDS); (2) New-to-Exporting Companies; (3) Capital Projects Bidding; and (4) Trade Association Activities. The Marketing Development Strategies (MDS) focuses on providing financing to smaller Canadian exporting firms for the development of simple marketing plans concentrating on the development of a particular foreign market. The Capital Projects Bidding assists Canadian exporters with the preparation of bids and contractual proposals for major capital projects in foreign countries. Trade Association Activities is a program designated to assist Canadian trade and industry associations develop export market development strategies.

Before submitting an application for PEMD financing, the PEMD encourages companies to obtain relevant information about the proposed market from a Trade Commissioner or a specialist with the Canadian embassy or consulate located in the particular market. Companies can obtain a Director of the Canadian Trade Commissioner Service from the International Trade Centres or from DFAIT's InfoCentre.

Once the company obtains this requisite information, the exporter next submits an application to a project officer. The project officer evaluates the proposal according to established PEMD eligibility criteria. Every approved application has a legal agreement that the applicant exporter and the Government of Canada both sign. This agreement

117. Information about the PEMD was obtained from the web-site of the Canadian government's Department of Foreign Affairs and International Trade, (visited Jan. 12, 1998) <<http://www.dfait-maeci.gc.ca/english/trade/handbook/goal.htm>>.

details assisted activities, the activity period, eligible costs, the target market, revenue and sales reporting requirements, terms of repayment, and other conditions. If the exporter has an existing legal agreement covering the market area, the exporter must report all revenue and sales in the market, and the PEMD will use this information in establishing the repayment terms of the financing.

C. CANADIAN PRIVATE SECTOR.

Through a joint venture of the Bank of Montreal (BMO) and Royal Bank of Canada, a company called Northstar Trade Finance Inc. has been formed recently. Northstar works in collaboration with the EDC, Western Economic Diversification, the Governments of British Columbia and Ontario, the Dalhousie Financial Corporation, and the Bank of Montreal.¹¹⁸ Northstar offers financing to foreign buyers of eligible Canadian goods and services at commercial rates¹¹⁹ and specializes in lending to SMEs who need export sales financing for transactions in amounts between C\$100,000 and C\$3 million, with repayment terms of one to five years.¹²⁰ While Northstar works primarily with exporters of capital goods and services, it is also open to working with other types of businesses.¹²¹

Northstar offers medium-term loans to foreign purchasers of Canadian goods and services provided that the goods and services have at least fifty percent Canadian content or added value. Northstar pays the exporter and then collects from the buyer over a period of up to five years.¹²²

In addition to this program, Northstar also offers a Floor Plan Finance program that enables exporters to sell through foreign distributors to whom the exporter extends credit. Northstar pays the exporter upon shipment, and is repaid with interest by the approved distributor either upon sale of the goods or in 360 days, whichever comes first.¹²³

V. Export Financing Options for Mexican Exporting Firms.

A. OVERVIEW OF THE MEXICAN ECONOMIC SITUATION.

Mexico's two primary export financing agencies are Nacional Financiera (NAFIN) and Bancomext. Both of these institutions possess the capabilities to make loans to Mexican exporters, offering programs categorically similar to those of their American and Canadian counterparts. While making export financing options available to Mexican exporters, NAFIN and Bancomext's greatest challenge in recent times has been to find either Mexican business projects to finance or Mexican businesses with sufficient confi-

118. Graham Clayton, *Financial Advice for Exporters*, N. ONTARIO BUS., May 1, 1997, at 4A, available in 1997 WL 9087436.

119. *Royal Bank-Northstar: Joins Forces with Bank of Montreal*, DOW JONES NEWS SERVICE, Aug. 28, 1997.

120. *Id.*

121. Clayton, *supra* note 118.

122. *Id.*

123. *Id.*

dence to add to their existing debt burdens.¹²⁴ In addition to the lack of demand by credit-worthy borrowers, Mexican lenders are gun-shy from Mexico's financial crisis that followed the December 1994 peso devaluation. One Mexican banker asserted that many Mexican banks are not lending because "fundamental problems of [the] financial crisis have yet to be completely fixed; [for example] bankruptcy processes . . . still favor borrowers more than lenders, and credit information is poor."¹²⁵ Mexico's development banks work primarily through the country's commercial banks; however, apart from the infrastructure problems, commercial banks recently have been more preoccupied with renegotiating their past-due loan portfolios than with the promotion of export financing.¹²⁶

Mexico's recovery is being led by export-oriented firms, so the potential for Bancomext and NAFIN financing is undoubtedly present.¹²⁷ Nevertheless, these exporting businesses do not look to these agencies for financing. Rather, Mexican exporters predominantly finance "investments and inventories from profits or, in the case of the largest companies, borrowings from foreign banks."¹²⁸ In 1996, foreign banks extended approxi-

124. *Mexico Development Banks Struggle to Provide More Credit*, DOW JONES NEWS SERVICE, Aug. 5, 1997.

125. Craig Torres, *Economists Project Mexican Slowdown As Credit Crunch Threatens Recovery*, WALL ST. J., Jan. 22, 1997, available in 1997 WL-WJS 2406560 (citing Mr. John Detmold, chairman and chief executive of Bank Quadrum, S.A.). Top Mexican officials are aware of these problems; President Zedillo in April promised to continue Mexico's support to its exporting sector, stating that "the public and private sectors will continue 'joining forces' to accelerate deregulation, develop the country's infrastructure and reform its institutions." F. Brinley Bruton, *Zedillo Pledges to Support Exports*, THE NEWS, Apr. 23, 1997, available in 1997 WL 8252095. For a relatively recent discussion of recent reforms in the Mexican financial sector, see *Financial Sector & Pension Reform*, LATINFINANCE, Sept. 1, 1996, at M31, available in 1996 WL 9952065. See also Kal Kaplan Carlos Albarran, *Navigating the Mexican Maze: Import/Export Promotion Through Factoring (Latin America Trade Finance 1996-1997)*, LATINFINANCE, Sept. 1, 1996, at T4, available in 1996 WL 9952071. "Mexican law is generally protective of the debtor, and . . . many attempts to collect debts have been hung up in the Mexican court system for years. Fortunately, these delays have been ameliorated to some extent by a May 1996 government act that cancels many long-standing appeals favorable to debtors." *Id.*

126. Torres, *supra* note 125.

127. "Exporting is not easy, above all for small business, but we also know that there isn't a better alternative to achieve quick and sustainable growth." Bruton, *supra* note 125 (quoting Enrique Vilatela, Bancomext Director General). Between 1982 and 1996, "Mexico has transformed itself from a mono-exporting country that depended heavily on the international price of oil to one with a diverse set of manufactured goods making up 84 percent of foreign sales." *Id.* (quoting Mexico's Commerce Secretary Herminio Blanco). President Ernesto Zedillo cites further figures regarding this shift in Mexico's exporting emphasis: "[i]n 1985, exports made up a mere 24 percent of the country's gross domestic product (GDP), whereas in 1996 exports equaled 55 percent of GDP. At the same time, the value added of the export sector went from 11 percent to 27 percent of GDP." *Id.*

128. Torres, *supra* note 125. See also *Mexico Development Banks: Waiting for Domestic Recovery*, DOW JONES NEWS SERVICE, Aug. 5, 1997. About 30,000 Mexican companies are involved in exporting, however, only 300 of these account for seventy percent of all of Mexico's exports, which are expected to total \$110 billion in 1997. *Mexican Foreign Trade Bank Announces Loans for Small Firms*, DOW JONES INT'L NEWS, Oct. 16, 1997. Other factors for the lack of demand of credit are a lack of "capacity or the size to work with large markets." *Mexico Development Banks: Direct Dealings with Clients*, DOW JONES NEWS SERVICE, Aug. 5, 1997 (quoting Abel Jacinto, vice-president of Bancomext).

mately \$3.5 billion in credit to private enterprises in Mexico, according to Capital Data Ltd., London.¹²⁹

Apart from loans from foreign banks, trade finance in Mexico historically has been accomplished through three methods, however only one of these methods is a financing option offered through either Bancomext or NAFIN. The first financing method is through the use of lines of credit, which typically come in three types: "a global line of credit, a short-term line of credit or an individual letter of credit (LC) for a specific transaction."¹³⁰ Bancomext and NAFIN offer both lines of credit and letters of credit. Lines of credit and letters of credit are prohibitively expensive, however, both because of high interest rates in Mexico and the fees for creating and managing LCs, which "add a considerable cost to every transaction."¹³¹ The second method of financing is open account terms offered directly by Mexican businesses. Few Mexican businesses, however, have the capacity to offer open terms to any purchaser "except to [those] largest and most well-established buyers."¹³² The third method of trade finance is through factoring, where a lending institution will either purchase accounts receivables from a Mexican business at a discounted price or use accounts receivables as collateral for loans to the business. This option is available only through commercial lending institutions in Mexico.¹³³

B. NACIONAL FINANCIERA.

Nacional Financiera (NAFIN) is Mexico's government-owned development bank.¹³⁴ NAFIN, which works primarily with small-to medium-sized companies, loaned 10.4 billion pesos in the first half of 1997, while its budget for the year is 35 million pesos.¹³⁵

129. Torres, *supra* note 125.

130. Albarran, *supra* note 125.

131. *Id.*

132. *Id.*

133. *Id.* This article asserts that factoring first became available after the bank nationalization in Mexico in 1982. Banks focused on "using their assets to support large public companies and the government" and factors began to develop as financial service providers independent of banks. *Id.* As the article states:

Within Mexico, factors provide a large share of short-term operating capital. Factoring there is widespread, and may include asset-based lending. For example, factors may offer inventory loans, more typically provided in other countries by banks. Beyond industries in the US that traditionally use factors, such as apparel, textiles, and home furnishing, factors in Mexico also serve other industries—automotive parts, chemicals, consumer and commercial electronics, food, plastics, and steel.

The prevalence of accounts receivable factoring is boosted by the fact that it is the only financial service not subject to Mexico's fifteen percent value-added tax (VAT). In addition, factoring companies are better positioned legally than other entities to recover what is owed them, even in bankruptcy situations.

Id. As a point of comparison, the United States Ex-Im Bank's Working Capital Guarantee Program can make use of accounts receivable as collateral. See *supra* text accompanying note 36.

See also text accompanying note 93 concerning the EDC's MARG Program.

134. *Nacional Financiera*, (visited Feb. 17, 1998) <<http://www.nafin.gob.mx>> [hereinafter NAFIN].

135. *Mexico Development Banks Struggle to Provide More Credit*, *supra* note 124.

NAFIN had planned to provide credit to as many as 18,000 companies in 1997, but by the end of June 1997, it had only extended credit to 3,500 companies.¹³⁶

NAFIN arranges short, medium, and long-term credit operations to assist Mexican enterprises on their specific needs for raw materials and capital goods, technological improvements and development, the building and renovation of manufacturing facilities, the hiring of consultant services, and investments related to pollution control or environmental protection.¹³⁷ NAFIN channels these financial resources through commercial banks and other non-banking financial intermediaries.¹³⁸ These financial institutions are responsible for the initial evaluation of a borrower's creditworthiness using criteria promulgated by NAFIN. NAFIN performs its own feasibility analysis in cases of large or complex transactions. NAFIN loans for working capital have terms ranging from five to six years. In the case of loans for the financing of capital goods or manufacturing facilities, the terms could be up to twenty years. Most of NAFIN's loans bear interest at floating rates and since April 1994, loans in pesos are tied to the TIIE¹³⁹ plus the spread or margin charged by the financial intermediary.

1. Credit Lines For Foreign Trade.

Trade finance may take the form of loans for specific projects that will generate imports of capital goods into Mexico or foster exports of goods and commodities to Mexico's trading partners. Regarding imports, NAFIN generally issues letters of credit to foreign suppliers. To fund the export financing operations, NAFIN has established dedicated lines of credit with financial institutions from different countries. NAFIN also takes direct loans from official export credit agencies. Foreign currency loans reflect the terms and conditions obtained in the international financial markets. Dollar denominated loans generally bear interest rates equal to the London Inter-Bank Offered Rate (LIBOR),¹⁴⁰ plus a spread.

NAFIN primarily seeks currency matching in its foreign trade operations. Thus, it generally requires the financial intermediary to ensure that the ultimate borrower has access to foreign currency earnings or is appropriately hedged.

2. Direct Lending Program.

Under this program, loans are directly authorized and granted by Nacional Financiera to finance specific projects of all types of enterprises, primarily in the manufacturing sector. The Direct Lending Program has as its primary purpose the financing of manufacturing projects undertaken by new companies or the financing of renovation and moderniza-

136. *Mexico Development Banks: Direct Dealings with Clients*, *supra* note 128. Further quantifying this lack of demand, "[i]n 1994, Nafin channeled credits through 340 credit unions; it now works with only 55." *Id.*

137. NAFIN, *supra* note 134, at <<http://www.nafin.gob.mx/lending.html>>.

138. These are institutions "[s]uch as credit unions, leasing companies and factorage agencies, among others." NAFIN, *supra* note 134, at <<http://www.nafin.gob.mx/glossary.html>>.

139. This is the "Interbank Equilibrium Interest Rate . . . [which is] based on the cost of money in . . . transactions among [M]exican commercial banks, . . . published daily by the Central Bank - Banco de Mexico." *Id.*

140. *Id.*

tion of existing firms. As NAFIN states, the purpose of this program is to promote the development of suppliers, the creation of employment, and the improvement of the economy's foreign trade sector.

The financing under the Direct Lending Program must specifically be for equipment imports to modernize these companies' manufacturing processes. The firms must have subscribed supply agreements with public sector entities,¹⁴¹ or engage in activities that either promote other supplier's distribution schemes or foster the creation of newfound production chains.

The terms and conditions of loans granted through this program, either for the acquisition of fixed assets or for permanent working capital needs, are determined on a case-by-case basis and depend on the financing period agreed upon and the risk assumed by NAFIN. The term may be for up to twenty years, including a maximum grace period of three years. Interest rates are based on the TIIE in the case of loans denominated by Mexican pesos or on the LIBOR for U.S. Dollar denominated transactions.

3. *Guarantees Program.*

NAFIN also has a Guarantees Program which guarantees loan obligations undertaken by micro-, small-, and medium-sized enterprises seeking to access domestic sources of funds from commercial banks. In general NAFIN's guarantee for any individual loan will not exceed fifty percent of the loan amount, however, this percentage increases for loans for the financing of technology improvements or environmental projects; these can be guaranteed up to eighty percent, seventy-five percent, and seventy percent, for micro and small-size, medium-size, and large-size enterprises respectively. Commissions are determined on a case-by-case basis, according to the proportion of the loan being guaranteed and the level of risk involved in the financing.

C. *BANCOMEXT*¹⁴² (BANCO NACIONAL DE COMERCIO EXTERIOR).

Bancomext is the Mexican Government's development bank and financial institution responsible for the promotion of foreign trade investment and joint-venture opportunities between Mexican and foreign companies. Founded in 1937, Bancomext is headquartered in Mexico City and has forty-one regional offices throughout Mexico. Bancomext functions as a credit institution and provides trade financing products and services to Mexican companies with the goals of developing foreign trade projects and enhancing the presence of Mexican domestic products in international markets.¹⁴³ Bancomext provides financing to increase Mexico's range of goods available for export. Services provided by the bank include the extending of export and import credits for non-oil goods and services. Bancomext also offers loan guarantees to protect against non-payment risks in foreign

141. These public sector entities include: "Petróleos Mexicanos, Instituto Mexicano del Seguro Social (IMSS), Sistema de Transporte Colectivo and Comisión Nacional de los Libros de Texto Gratuitos." *Id.*

142. See generally *Bancomext* (visited Feb. 17, 1998) <<http://www.bancomext.gob.mx>>. Information regarding Bancomext was provided to the author by the Trade Commission of Mexico's Dallas office, 2777 Stemmons Freeway, Suite 1622, Dallas, Texas 75207. The Trade Commission of Mexico can also be contacted at (214) 688-4095.

143. *Bancomext*, *supra* note 142.

trade. Bancomext's services are designed to meet the financing needs of both private and public sector enterprises, marketing firms, and "companies involved in manufacturing and marketing value-added goods and services in general, ranging from agricultural commodities to electronic products, automobile parts and services in fields such as tourism, engineering and construction."¹⁴⁴ Most of the bank's credit transactions are carried out through Mexico's commercial banks and the main sources of Bancomext funding come from its own capital, foreign credit, and funds derived from operations.¹⁴⁵

Bancomext's total budget for 1997 was \$10 billion and of this amount, it loaned \$2.5 billion in the first six months of 1997.¹⁴⁶ Bancomext's director general, Enrique Vilatela, has stated that Bancomext's goal for the future is to move away from the financing of larger companies and rather concentrate on helping smaller companies export.¹⁴⁷ Toward this end, Bancomext announced in October 1997 a new credit program designed to help small- and medium-sized firms that supply large exporters and state-owned companies.¹⁴⁸ In addition to making credit more available to smaller firms, Bancomext wants to see an increase in domestic content of export products.¹⁴⁹

Looking forward to finishing fiscal 1997, Vilatela stated that Bancomext expects to lend only \$5 billion of the \$10 billion it had available for credits.¹⁵⁰ Of the \$5 billion, only twenty percent was earmarked for small firms, with the rest going to large exporting companies.¹⁵¹ Mr. Vilatela acknowledges that Bancomext is presently undergoing changes to become more responsive to the needs of Mexican exporters, as it "seeks to consolidate itself as an 'authentic development bank'."¹⁵²

144. Information provided to the author by the Trade Commission of Mexico, Dallas office. See also Bancomext (Dallas) (visited Feb. 14, 1998) <<http://www.bancomextdallas.com/aboutus-nf.htm>>.

145. *Id.*

146. *Mexico Development Banks Struggle to Provide More Credit*, *supra* note 124.

147. *Mexico Export Sector: Mexico Recent Export Player*, DOW JONES INT'L NEWS, Apr. 21, 1997.

148. *Mexican Foreign Trade Bank Announces Loans For Small Firms*, *supra* note 128. Bancomext's program is consistent with a recent trend of small to mid-size companies who have tried to reduce their credit risk in export markets by "becoming the suppliers to large, successful exporters such as beer producer Grupo Modelo SA, petrochemicals producer Cydsa SA and copper giant Grupo Mexico SA." *Mexico Development Banks: Waiting for Domestic Recovery*, *supra* note 128.

149. *Mexican Foreign Trade Bank Announces Loans for Small Firms*, *supra* note 128.

150. *Id.*

151. *Id.*

152. Bruton, *supra* note 125. One recent development with Bancomext is its placement of \$350 million worth of commercial paper in the U.S. market in December 1997. The credit "was backed by 27 international commercial banks, with BankAmerica Robertson Stephens acting as the structuring agent and Barclays Bank issuing a letter of guarantee for the credit" and BankAmerica, Credit Suisse First Boston, JP Morgan and Lehman Brothers placing the paper. *Mexico Bancomext Places \$350M in Commercial Paper in U.S.*, DOW JONES INT'L NEWS, Jan. 12, 1998. Bancomext stated that the credit was over a two-year period, "with a risk commission of 40 basis points per year" and that "the credit would be used to address working capital needs of Mexican export companies." *Id.*

D. TRADE COMMISSION OF MEXICO (CONSEJERIA COMERCIAL DE MEXICO).

The Trade Commission of Mexico is Bancomext's promotional arm. With thirty-three offices around the world, including seven in the United States, the Commission acts as a liaison between Mexican exporters and foreign investors interested in pursuing opportunities in Mexico. The Commission has two programs designed to promote Mexican exports through the promulgation of information about Mexican businesses. The first is the Foreign Investment Assistance Program (FIAP). The purpose of FIAP is to assist foreign companies who are interested in forming strategic alliances, joint ventures or mergers with Mexican companies, or who are interested in direct investment in Mexico. The second program is the Trade Opportunities Program (TOP). TOP is designed to assist foreign companies either in importing products from Mexico or in representing Mexican companies abroad.¹⁵³

VI. Conclusion.

While this article has not exhaustively detailed all of the available export financing options available to businesses in the three NAFTA countries, it has attempted to give an overview of the major export financing and export market development programs offered by the governments of the United States, Mexico, and Canada. More information regarding these programs is available through the Internet, as that medium for the dissemination of information continues to become more widely used. This article provides a mere snapshot of the programs available at the time the article was written—early 1998. The reader is advised to use it only as a guide to start a search for an export financing program appropriate to their needs. Due to constant changes in the law, the development of new programs by these agencies, and the continued globalization of world markets, the programs listed here undoubtedly only represent a small fraction of the financial resources that will be available to exporters in the years ahead.

153. Information provided to the author by the Trade Commission of Mexico, Dallas office, *supra* note 142.
